

***United States Court of Appeals
for the
District of Columbia Circuit***



**TRANSCRIPT OF
RECORD**

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United States Court of Appeals for the
District of Columbia

APRIL TERM, 1937.

No. 6963

158

EDWIN H. BROWNLEY, STATUTORY RECEIVER,
WARDMAN REALTY AND CONSTRUCTION COM-
PANY, APPELLANT,

vs.

JULIUS I. PEYSER AND JOSEPH P. TUMULTY, RE-
CEIVERS, WARDMAN REAL ESTATE PROPER-
TIES, INC., AND WASHINGTON PROPERTIES,
INC.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR
THE DISTRICT OF COLUMBIA

LIBRARY

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United States Court of Appeals for the District of Columbia

APRIL TERM, 1937.

No. 6963

EDWIN H. BROWNLEY, STATUTORY RECEIVER,
WARDMAN REALTY AND CONSTRUCTION COM-
PANY, APPELLANT,

v.

JULIUS I. PEYSER AND JOSEPH P. TUMULTY, RE-
CEIVERS, WARDMAN REAL ESTATE PROPER-
TIES, INC., AND WASHINGTON PROPERTIES,
INC., APPELLEES.

DISTRICT COURT OF THE UNITED STATES FOR THE DISTRICT OF
COLUMBIA.

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United States Court of Appeals for the District of Columbia

1 United States Court of Appeals for the
District of Columbia

No. 6963

EDWIN H. BROWNLEY, Statutory Receiver, Wardman Realty
and Construction Company, *Appellant*,

v.

JULIUS I. PEYSER and JOSEPH P. TUMULTY, Receivers, Ward-
man Real Estate Properties, Inc., and WASHINGTON
PROPERTIES, INC., *Appellees*.

Endorsed: Filed May 3 1937 Charles E. Stewart, Clerk
District Court of the United States
for the District of Columbia

Equity No. 53,117

Equity No. 53,180

CENTRAL HANOVER BANK & TRUST Co., a body corporate, and
FRANK WOLFE, *Trustee*,

v.

WARDMAN REAL ESTATE PROPERTIES, INC., a body corporate.

RANDOLPH P. COMPTON,

v.

WARDMAN REAL ESTATE PROPERTIES, INC., a body corporate.

UNITED STATES OF AMERICA,
District of Columbia, ss:

BE IT REMEMBERED that in the District Court of the
United States for the District of Columbia at the
times hereinafter mentioned the following papers

were filed and proceedings had in the above entitled cause, to-wit:

- 2 *Agreed Statement of the Case to Constitute Part of the Record in the United States Court of Appeals for the District of Columbia.*

The following is a statement of the above entitled case showing how the questions involved arose and were decided in the District Court of the United States for the District of Columbia, and such portions of the pleadings, evidence and record which one or all of the parties hereto deem essential to a decision of the appeal by Edwin H. Brownley, statutory receiver, Wardman Realty and Construction Company, appellant, from the order entered February 19, 1937.

Statement.

I. Wardman Realty and Construction Company is a corporation organized under the laws of Maryland and owned all of the capital stock of the Wardman Real Estate Properties, Inc.

Wardman Real Estate Properties, Inc., is a corporation organized under the laws of Maryland, and acquired title to and held possession of the Wardman properties on October 2, 1928, in the District of Columbia. These properties were acquired from the Wardman Realty and Construction Company, and consisted of Wardman Park Hotel, Wardman Park Addition, 2700 Connecticut Avenue, Cathedral Mansions, Center, Cathedral Mansions, North, The Highlands Apartment, Carlton Hotel, Department of Justice Building and Davenport Terrace Apartments. These companies will hereafter be referred to herein as the Construction Company and the Properties Company. From October 2, 1928, through July 15, 1929, the properties were owned and operated by the Properties Company.

II. As of July 15, 1929, the Properties Company leased the properties to the Construction Company under and pursuant to the following lease:

3 THIS INDENTURE OF LEASE, made as of the 15th day of July, 1929, between WARDMAN REAL ESTATE PROPERTIES, INC., a corporation organized and existing under the laws of the State of Maryland (hereinafter referred to as the "Lessor"), and

WARDMAN REALTY AND CONSTRUCTION COMPANY, a corporation organized and existing under the laws of the State of Maryland (hereinafter referred to as the "Lessee"),

WITNESSETH:

That the Lessor, in consideration of the rents, covenants and agreements hereinafter reserved, contained and mentioned on the part of the Lessee, hereby grants, demises and leases to the Lessee, and the Lessee does hire and take from the Lessor, all those eleven (11) lots or parcels of land in the City of Washington, District of Columbia (together with all buildings, improvements and betterments thereon, and all personal property of the Lessor located therein or thereon except personal property currently carried as inventories on the books of the Lessor), more particularly described as follows:

FIRST.

Wardman Park Hotel.

* * *

SECOND.

Addition to Wardman Park Hotel.

* * *

THIRD.

Carlton Hotel.

* * *

FOURTH.

Highlands Apartments.

* * *

FIFTH.

Chastleton Apartments

* * *

SIXTH.

Cathedral Mansions.

* * *

SEVENTH.

Connecticut Avenue and Davenport Apartments.

* * *

EIGHTH.

Boulevard Apartments.

* * *

NINTH.

Stoneleigh Court.

* * *

TENTH.

Department of Justice Building.

* * *

ELEVENTH.

2700 Connecticut Avenue Apartment.

* * *

All of the foregoing premises are hereby granted, demised and leased, expressly subject, however, to the following (hereinafter sometimes collectively referred to as "the Mortgages" or "said Mortgages"); to-wit: (1) the prior lien of a certain mortgage and deed of trust dated as of September 1, 1928, and executed by the Lessor to Central Union Trust Company of New York and Frank Wolfe, as Trustees, securing an issue of First and Refunding Mortgage Gold Bonds issued and to be issued thereunder and secured thereby, limited in aggregate principal amount of \$16,000,000 at any one time outstanding, as well as the liens of any mortgages and deeds of trust securing any bonds, notes or other obligations issued by the Lessor for the purpose of refunding any of said First and Refunding Gold Bonds; (2) the prior lien of a certain mortgage and deed of trust dated as of September 1, 1928, and executed by the Lessor to The Riggs National Bank of Washington, D. C., as Trustee securing an issue of General Mortgage Gold Bonds issued thereunder and secured thereby, limited in aggregate principal amount to \$2,500,000 at any one time outstanding, as well as the liens of any mortgages and deeds of trust securing any bonds, notes or other obligations issued by the Lessor for the purpose of refunding any of said General Mortgage Gold Bonds; and (3) as to the respective properties covered thereby, to the liens of mortgages and deeds of trust having liens prior to that of said mortgage

and deed of trust mentioned in (1) above, as therein specified and permitted.

Subject, also, however, to existing covenants and restrictions of record, if any, affecting said premises insofar as the same are now in force and effect; to party walls and party wall agreements, if any, now in force and effect; and to all current leases now in force and effect, which current leases the Lessor does hereby assign to the Lessee, upon the condition, however, that if the Lessee shall be removed from the possession of said premises under the provisions of Paragraph Tenth hereinafter set forth, or if this Lease shall be terminated as to any part of said premises as hereinafter permitted, said assignment of any such current leases affecting such premises shall immediately become null and void and the interest of the Lessor therein shall be deemed to be and shall thereupon be assigned and revert to the Lessor hereunder.

5 TO HAVE AND TO HOLD the above mentioned and described premises (together with all buildings, improvements and betterments thereon, and all personal property of the Lessor located therein or thereon except personal property currently carried as inventories on the books of the Lessor), subject as aforesaid, unto the Lessee, its successors and assigns, from the 15th day of July, 1929, for a term of ten (10) years and sixteen (16) days next ensuing; yielding and paying for the same unto the Lessor, its successors or assigns, as rent, a sum sufficient to cover all interest and amortization (including sinking funds and so-called "curtails") requirements under said Mortgages and of the bonds and other obligations issued thereunder, and in respect of the Two Year 6% notes of the Lessor, due September 1, 1931, all as they severally accrue during such term, provided that such rent shall not be less than One Million five hundred thousand dollars (\$1,500,000.) yearly, except that such net rental shall be subject to reduction as hereinafter provided in paragraphs Fourteenth and Fifteenth hereof. The portion of such rent necessary to cover said interest and amortization requirements as aforesaid shall be payable by the Lessee unto the Lessor in advance, in an amount equivalent to each such charge, at least five (5) days before each such charge, respectively, becomes payable under the terms of the Mortgages, as

aforesaid, and of the bonds or other obligations issued thereunder. The portion of such rent, if any, in excess of such interest and amortization requirements in any year ending on the 15th day of July, shall be payable on the 15th day of the next succeeding month.

Said rental shall be paid to the Lessor at its office in the City of Washington, or to such other person or persons, or at such other place or places in said City as the Lessor, its successors or assigns may from time to time designate in writing.

In lieu of making such payments to the Lessor, the Lessee may, with the approval of the Lessor, pay from time to time, as they accrue, the portion of such rent necessary to cover said interest and amortization requirements, direct to the mortgagees or trustees under the Mortgages in question and deliver to the Lessor upon demand receipt therefor or other evidence thereof.

The rent reserved and stated in the foregoing paragraphs shall be net, and the Lessor shall not be called upon for any expenses, outlay or disbursements of any nature whatsoever in connection with carrying said properties or the operation or maintenance thereof.

It is hereby mutually covenanted and agreed that it is the intention hereof that the Lessor shall receive said rental free from all taxes, assessments and other similar obligations which, by the nature of this lease, are made payable by the Lessee, and that the Lessee, shall pay as additional rental all such costs, charges, expenses and damages which, except for the execution and delivery of this lease, would have been chargeable during said term against the demised premises and payable by the Lessor. The Lessee shall not, however, be obligated to pay the principal, at final maturity, of any of the Mortgages or of the obligations issued thereunder or the Two Year 6% Notes of the Lessor, due September 1, 1931.

This lease is made upon the foregoing and the following covenants, conditions and agreements, to wit:

First: The Lessee agrees that it will pay the rent as above and hereinafter provided and the additional rent hereinafter provided for.

Second: The Lessee agrees that it will make all repairs, renewals or replacements of every kind and nature, both

exterior and interior, and whether structural or otherwise, to all the demised premises, and all improvements thereto, including the roofs, sidewalks and shoring of walls of adjoining buildings, during the term of this lease, and keep all sidewalks free from snow and ice, and the Lessor shall not, during the term of this lease, be liable for any manner of repairs, renewals or replacements in or about any of the said premises or to any part of the said sidewalks or walls adjacent or appurtenant thereto; that it will not permit the said premises, or any part thereof, to be used for any business which may be offensive or dangerous or which may become a nuisance or may be in violation of law; that it will not permit the said premises, or any part thereof, to be occupied or used for any business deemed extra-hazardous on account of fire; that it will not suffer or permit any act or thing which would violate the conditions of or invalidate the fire insurance policies covering the said premises, or by which the recovery of the insurance moneys thereon might be hindered or impaired; that it will observe and comply with, and be responsible for, and shall bear all expense in the observance of and compliance with each and every statute, ordinance, rule, regulation, notice, and notice of violation now in force or hereafter enacted or issued by or of any governmental authority and/or of any and all bureaus and departments, applicable to and affecting the demised premises and each and every part thereof, including structural changes as well as the use and occupation thereof, and the sidewalks, curbs, gutters and streets, and vaults under the sidewalk and sewer, water, gas and other connections beyond the building line, and shall likewise comply with all rules and regulations of the Board of Fire Underwriters in the District of Columbia or of such other Board of Fire Underwriters as may have jurisdiction over said premises, whether or not structural changes shall be required by such ordinances, rules, regulations and requirements; and that

7 the said Lessee shall be liable for and shall save harmless the said Lessor of and from any loss incurred or any penalty, claim or damage imposed, made or recovered, and from any liability to any person in consequence of injuries sustained by reason of the neglect of the Lessee to observe said ordinances, rules, regulations and requirements as aforesaid; that throughout said term

it will permit at all times during business hours the Lessor and representatives of the Lessor to enter the demised premises for the purpose of inspection, suffer the Lessor to make repairs and improvements to all parts of the buildings and to comply with all lawful orders and requirements of governmental authority applicable to said buildings or to any occupation thereof, after failure or default by the Lessee so to do, and to exhibit them for purposes of rental; forever indemnify and save harmless the Lessor from and against any and all liability, penalties, damages, expenses and judgments arising from injury during said term to person or property of any nature and howsoever caused, and also for any matter or thing growing out of the occupation of the demised premises by the Lessee or of the use by the Lessee (or by persons with whom it deals) of the streets, sidewalks or vaults adjacent thereto; repair, at or before the end of the term, all injury done by the installation or removal of movable fixtures, furniture and property; and, at the end of the term, quit the demised premises with all alterations, additions and improvements in good order and condition, reasonable wear and tear excepted.

Third: The Lessee agrees that it will pay and discharge, within thirty (30) days after the same shall have been due and payable, all duties, assessments, taxes, water rates, and all other payments and charges of every kind and nature whatsoever, extraordinary as well as ordinary (not including, however, income, inheritance, devolution, estate or gift taxes) which shall or may, during the term hereby granted, be levied, charged, assessed or imposed upon or against said premises, or any part thereof, so that the premises demised and the interest of the Lessor thereunder shall, so far as it lawfully may be done, be free from all such duties, water rates, taxes, assessments, payments and charges aforesaid, and that this agreement shall yield the Lessor not less than the rent reserved upon the annual basis contained throughout the term hereof, and shall at any and all times, upon demand of the Lessor, furnish to it for inspection and for such use as may be proper in protecting its estate in the premises, the receipts or other written evidence of such payments.

All current items, including but not limited to, insurance, water rents, taxes, current accounts, inventories and other like items, as well as interest and amortization payments under the Mortgages, as aforesaid, shall be adjusted as of the respective dates of the inception and termination
8 of this lease in accordance with approved accounting practice.

Fourth: The Lessee agrees that it will, as part of the consideration of this lease, and during the term hereby demised, keep all buildings and improvements upon the demised premises, insured against loss or damage by fire or otherwise, and will carry insurance against other risks, with policies of the character and in amounts and otherwise as required by the respective Mortgages to which this lease is expressly subject, so as to comply with each and every requirement with respect to insurance, contained in said Mortgages.

* * *

Tenth: If the Lessee shall make default in the payment of rent, or if the demised premises, or any of them, shall become abandoned or deserted, the Lessor may give the Lessee fifteen (15) days' written notice of such default or of such mentioned act and of the Lessor's intention to end the term of this lease; or if the Lessee shall be adjudicated a bankrupt, or shall make a general assignment, or take the benefit of any insolvent act, or if a receiver or trustee be appointed for the Lessee's property, or if a petition in bankruptcy shall be filed by or against the Lessee, the Lessor may give the Lessee thirty (30) days' written notice of such default or of such mentioned act and of the Lessor's intention to end the term of this lease; or if the Lessee shall make default in fulfilling any of the covenants of this lease other than hereinbefore in this paragraph mentioned, the Lessor may give the Lessee sixty (60) days' written notice of such default and of the Lessor's intention to end the term of this lease; and if such default shall not have been cured or obviated within said fifteen (15) days, or thirty (30) days, or sixty (60) days, as the case may be, then, at the expiration of said fifteen (15) days, thirty (30) days, or sixty (60) days, as the case may be; or, in case of notification in writing to the Lessor and the Lessee by the Trustee,

or by the holders of Twenty-five per cent. (25%) in principal amount of 6½% Gold Debentures of the Lessee then issued and outstanding, under the Lessee's Indenture to American Exchange Irving Trust Company as Trustee, dated as of September 1, 1928, of the happening and the continuance of an event of default as set forth in Section 1 of Article VI of said Indenture, the term under this lease shall expire as fully and completely as if that were the date herein definitely fixed for the expiration of the term and the Lessee will then quit and surrender the demised premises to the Lessor, but the Lessee shall remain liable as herein-after provided. If the notice last above provided for shall have been given and said fifteen (15) days, thirty (30) days, or sixty (60) days' period, as the case may be, shall have elapsed without said default having been cured or obviated, the Lessor may immediately or at any time thereafter re-

9 enter the demised premises and remove all persons and all or any property therefrom, either by summary dispossession proceedings or by any suitable action or proceeding at law, or by force or otherwise, without being liable to indictment, prosecution or damage therefor, and repossess and enjoy said premises, together with all additions, alterations and improvements. The Lessor may after obtaining possession of said premises re-let the same or any part thereof for the whole or any part of the term herein demised, from time to time as the Lessor may deem best, and may, should the Lessor deem it advisable, alter or subdivide the premises hereby demised for the purpose of re-letting the same. In the event that the Lessor shall obtain possession by re-entry, dispossession, summary proceedings or otherwise, the Lessee hereby agrees to pay to the Lessor on demand the expense incurred by the Lessor in obtaining possession of said premises, including legal expenses and attorneys' fees, and to pay such other expenses as the Lessor may incur in putting the premises in good order and condition, and any other expense or commissions which may be paid by the Lessor in and about the letting of the same. The Lessee further agrees to pay each month to the Lessor the deficit accruing from the difference between the amount to be paid as rent as herein reserved and the amount of rent which shall be collected and received

from the demised premises for such month during the residue of the term herein provided for after the taking possession by the Lessor; the overplus, if any, at the expiration of the full term herein provided for shall be paid to the Lessee unless, within the period of six (6) months from the termination of this lease, as in this paragraph provided, the Lessor shall, by a notice in writing, release the Lessee from any and all liability created by this clause of paragraph Tenth which it is agreed the Lessor shall, at the Lessor's option, have the right to do, in which event it is agreed that the Lessor and the Lessee shall have no further rights and liabilities hereunder. The Lessor may sue for and enforce the collection by law of such amount as above provided for which may be due at the expiration of each month and the Lessee expressly agrees that any such suit shall not be a bar to or prejudice in any way the rights of the Lessor to enforce the collection of the amount due at the end of any other future month by a like or similar proceeding. The Lessee hereby expressly waives any and all right of redemption in case the Lessee shall be dispossessed by judgment or warrant of any court or judge. The words "re-enter" and "re-entry" as used in this lease are not restricted to their technical legal meaning. The words "summary proceedings" as used in this lease shall be deemed to include and refer to any actions provided for under the laws applicable to the District of Columbia which shall be of the nature similar to "summary proceedings" provided for under the laws of the State of New York.

10 And the Lessee hereby waives and relinquishes unto and in favor of the Lessor the operation of all laws which do now, or hereafter may, exempt any property on the demised premises, or any property in any way belonging to the Lessee, whether on the demised premises or elsewhere, from levy and sale, upon distress for the rents or sums of money hereby reserved, or upon an execution on any judgment obtained in an action brought for nonpayment of rent, or for breach of any other of the within named conditions; and the operation of all laws which do now or may hereafter require the appraisal of any property in any distraint proceedings or notice to Lessee in such proceedings, Lessee hereby waiving its right to such notice.

In addition to any right or remedy hereinbefore in this paragraph given to the Lessor in case of any default by the Lessee, should the Lessee fail or omit to pay the rents or sums hereby reserved on the dates when the same are made payable, and such default shall not have been remedied in the time hereinbefore provided and the notice hereinbefore provided for shall have been given (and time in this case is understood and agreed to be of the essence of the contract, and not to be relieved against), or shall in any other respect violate any of the conditions and covenants herein contained and such default shall not have been remedied in the time hereinbefore provided and the notice hereinbefore provided for shall have been given, and the term under this lease thereby expires when the lease shall be so terminated by condition broken and notice as aforesaid; then it shall be lawful for any attorney, as attorney for the Lessee, to sign an agreement for entering in any competent court an amicable action and judgment in ejectment without any stay of execution against the Lessee and all persons claiming under it for the recovery by the Lessor of the possession of the hereby demised premises, for which this shall be a sufficient warrant; whereupon, if the Lessor so desires, a writ of *habere facias possessionem* shall issue forthwith without any prior writ or proceeding whatsoever, the Lessee hereby releasing and agreeing to release the Lessor from all errors and defects whatsoever in entering such action or judgment, or causing such possessory writ to be issued in any proceeding thereon or concerning the same, *provided*, that the Lessor shall first cause to be filed in such action an affidavit made by it, or someone on its behalf, setting forth the facts necessary to authorize the entry of such judgment according to the terms of this Lease, of which facts such affidavit shall be conclusive evidence, and if a true copy of this lease (and of the truth of the copy such affidavit shall be sufficient evidence) shall be

11 annexed to such affidavit, it shall not be necessary to file the original as a warrant of attorney, any rule of court to the contrary notwithstanding. No such determination of this lease, nor taking or recovering possession of the premises shall deprive the Lessor of any remedy or action against the Lessee, for rent or for damages for the

breach of any covenants herein contained; nor shall the bringing of such action for rent or breach of covenant, nor the resort to any other remedy herein provided for the recovery of rent or damages for such breach, be considered as a waiver of the right to insist upon a forfeiture, and obtain possession in the manner hereinabove provided. And *provided* further: That if for any reason after any such action has been commenced the same shall be determined and the possession of the premises remain in or be restored to the Lessee, the Lessor shall have the right in the event of any subsequent default or defaults, to bring one or more amicable actions in manner and form as hereinbefore set forth, to recover possession of said premises for such subsequent default.

Eleventh: In case the Lessor shall fail to make any payment of principal or of installment of principal, or of interest, which may become due upon any of said Mortgages, the Lessee may, if it so desires, pay the same to the holder of such Mortgage and thereupon be subrogated to the rights of the Mortgagee or Mortgagees or bondholder or bondholders to whom or for whose account the same shall be paid, and in addition thereto the Lessee may either deduct from any amount of rent then due or which may become due from time to time thereafter under this lease, any amount so paid, with interest thereon from the time of such payment, and any costs or charges which may have been paid by the Lessee which arise from the failure of the Lessor to make such payments, or may recover such amount or amounts from the Lessor in any manner that may be permitted by law.

Twelfth: The Lessor hereby covenants and agrees that the said Lessee, upon paying the rent herein reserved and performing and observing the covenants upon the part of the Lessee to be performed as herein provided, shall and may, at all times hereafter, peaceably hold and enjoy the said premises for the term hereby demised, without any let, interruption or disturbance whatever from the Lessor or anyone claiming by, through or under said Lessor.

* * *

12

Eighteenth: By resolution unanimously adopted by the affirmative vote of all of the directors of the

Lessor, its vice-president, James D. Hobbs, is hereby made, constituted and appointed the attorney in fact of said Company, Wardman Real Estate Properties, Inc., for and in its name, stead and place and on its behalf, to acknowledge this instrument as the deed of said Company and its execution and authorization as the lawful and binding deed of the said Company, pursuant to the laws of the District of Columbia, to enable and to permit the same to be admitted to record, and recorded pursuant to the laws of the District of Columbia as a lease of real estate and as a lease of chattels, in the office of the Recorder of Deeds for the District of Columbia; and do hereby ratify, approve and confirm any and all acts of said attorney in the premises.

Nineteenth: By resolution unanimously adopted by the affirmative vote of all of the Directors of the Lessee, its Vice President, Thomas P. Bones, is hereby made, constituted and appointed the attorney in fact of said Company, Wardman Realty and Construction Company, for and in its name, stead and place and on its behalf to acknowledge this instrument as the deed of said Company, and its execution and authorization as the lawful and binding deed of said Company, pursuant to the laws of the District of Columbia, to enable and to permit the same to be admitted to record and recorded, pursuant to the laws of the District of Columbia, as a lease of real estate and as a lease of chattels, in the office of the Recorder of Deeds for the District of Columbia, and do hereby ratify, approve and confirm any and all acts of said attorney in the premises.

IN WITNESS WHEREOF, the parties hereto have caused these presents to be signed by their respective Presidents or Vice Presidents and their corporate seals to be hereunto affixed and the same to be attested by the signature of their respective Secretaries or Assistant Secretaries, all as of the day and year first above written.

WARDMAN REAL ESTATE
PROPERTIES, INC.,
By JAMES D. HOBBS

(Corporate Seal)

Vice President.

Attest:

ROBERT N. TAYLOR
Assistant Secretary.

WARDMAN REALTY AND
CONSTRUCTION COMPANY,
By THOMAS P. BONES

(Corporate Seal)

Vice President.

Attest:

HUBBERT R. QUINTER

Secretary.

(Acknowledgment)

13 III. From the date of the aforementioned lease until February 26, 1931, the properties were operated by the Construction Company. On February 28, 1931, the Construction Company was in default to the Properties Company under said lease in the payment of rent specified therein in the amount of \$654,000., and there had accrued certain real estate taxes against said properties which were unpaid, but which the Construction Company was obligated to the Properties Company to pay, in the sum of approximately \$47,000. The Construction Company also had not paid personal taxes assumed by it, and claimed by the District of Columbia, in the sum of approximately \$30,000.

IV. Until February 26, 1931, the officers and directors of the Properties Company and Construction Company were identical. As of said last mentioned date the officers of the two companies were: J. R. Lane, President; G. E. Allen, Vice-President; T. R. Leavell, Treasurer, and L. M. Hodges, Secretary. On February 25, 1931, the officers of the Properties Company resigned, whereupon Thomas D. Carson was elected President of the Properties Company in place of J. R. Lane, and Humphrey Lloyd was elected Treasurer of the Properties Company in place of T. R. Leavell. J. R. Lane, G. E. Allen and A. C. Torgeson also resigned as directors of the Properties Company (but not of the Construction Company) and their places as directors of the Properties Company were filled by J. C. Stephens, Humphrey Lloyd and L. M. Hodges.

V. Immediately prior to the aforesaid severance of officers and directors between the Construction Company and the Properties Company and after such change had been carried into effect, negotiations were being carried on between those officers who remained exclusively officers of the Properties Company and those who remained exclusively

officers of the Construction Company for a cancellation of the lease between the two companies; in said negotiation those who thereafter were officers of the Construction Company were advised by counsel independent of the counsel for the Properties Company; and on March 7, 1931, an agreement was entered into between the two companies for cancellation of said lease, effective as of February 28, 1931, which agreement was, in so far as is material hereto, as follows:

MEMORANDUM OF AGREEMENT Made and entered into this 7th day of March, 1931, by and between WARDMAN REAL ESTATE PROPERTIES, INC., a corporation under the laws of the State of Maryland (hereinafter for convenience called the "properties Company") party of the first part, and WARDMAN REALTY AND CONSTRUCTION COMPANY, a corporation under the laws of the State of Maryland (hereinafter for convenience called the "Construction Company") party of the second part.

WHEREAS, the Construction Company has heretofore been lessee from the Properties Company for a term of years ending July 31, 1939, of the following properties:

Wardman Park Hotel
Addition to Wardman Park Hotel
Carlton Hotel
Highlands Apartments
Chastleton Apartments
Cathedral Mansions
Connecticut Avenue and Davenport Apartments
Boulevard Apartments
Stoneleigh Court
Department of Justice Building
2700 Connecticut Avenue Apartment

hereinafter for convenience collectively called the "Properties", under an Indenture of Lease between them dated as of July 15, 1929, and recorded among the land records of the District of Columbia in Liber 6349 at Folio 261, but said Construction Company has been in default in the payment of the rentals specified in said lease; and

WHEREAS, the Board of Directors of the Properties Company and the Board of Directors of the Construction Company have heretofore authorized the termination and cancellation of said lease effective as of the close of

15 business February 28, 1931, upon the terms, covenants and conditions and for the considerations set forth herein.

NOW THEREFORE in consideration of the cancellation of the aforesaid lease as hereinafter more fully set forth, and in further consideration of the assumption of certain liabilities of the Construction Company by the Properties Company as hereinafter set forth;

1.

The Construction Company does hereby:

1. Assign, pay over, transfer and deliver to the Properties Company all operating cash pertaining to the "Properties" and held by Hotels Management and Securities Corporation, Agent, as at the close of business February 27, 1931, and as more fully set forth on a schedule hereunto annexed and marked Schedule A-1. (And the Properties Company does hereby acknowledge receipt of the amount shown on said Schedule A-1);

2. Assign, pay over, transfer and deliver to the Properties Company all operating cash pertaining to the "Properties" and received by Hotels Management and Securities Corporation, as Agent, on February 27, and 28, 1931, and more fully set forth on a schedule hereunto annexed and marked Schedule A-2. (And the Properties Company does herein and hereby acknowledge receipt of the sums shown on said Schedule A-2):

3. Sell, transfer and deliver to the Properties Company all inventories of merchandise and supplies on hand and in transit and located in or upon the "Properties" as of the close of business February 28, 1931, as more fully set forth and described in a schedule hereunto annexed and marked Schedule B:

16 4. Assign, transfer and deliver to the Properties Company such deferred and prepaid items, applicable solely to the "Properties", as of the close of business February 28, 1931, as may be designated by the President of the Properties Company and set forth on a schedule to be annexed, as soon as available, to this agreement and marked Schedule C:

5. Sell, assign and transfer to the Properties Company the accounts receivable listed and set forth on a schedule

hereafter to be prepared and to be annexed hereto and marked Schedule D. (The parties hereto being unable now to affix said schedule to this agreement for the reason that the accountants of the Company are unable at this time to report exactly thereon). The particular accounts receivable to be listed and set forth upon said schedule shall be designated and specified within 20 days from date hereof, by the President of the Properties Company and the President of the Construction Company from the accounts receivable of the Hotels Management and Securities Corporation as Agent for the Construction Company, as of the close of business February 28, 1931, which have accrued from the operation of the "Properties" and they shall fix the appropriate "reserves" therefor. The total face amount, after the deduction of the said "reserves", of said accounts receivable when selected shall be equal to:

(a) The amount of the accounts hereby assumed and to be set forth on Schedule E, as hereinafter described, when prepared and annexed hereto, plus the amount of the accrued liabilities and accrued real estate taxes hereby assumed and to be set forth on Schedules F and G, hereinafter referred to, when prepared and annexed hereto:

LESS

(b) The sum of the cash set forth in Schedules A-1 and A-2 hereof, the net amount of the inventories set forth in Schedule B and the amount of the deferred and prepaid items set forth on Schedule C.

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II.

The Properties Company does hereby:

1. Assume and agree to pay certain operating accounts payable of the Construction Company and/or of its agent, Hotels Management and Securities Corporation, arising wholly and solely out of the operation of the "Properties" and due and payable as of February 28, 1931, and as particularly set forth on a schedule hereafter to be prepared and to be annexed hereto and marked Schedule E. (The parties hereto being unable now to affix said schedule to this agreement for the reason that the accountants of the Company are unable at this time to report exactly thereon). The particular accounts payable to be set forth on said schedule shall be selected within 20 days from date hereof

by the President of the Properties Company from accounts payable of the Construction Company as of the close of business February 28, 1931, which have accrued from the operation of the "Properties"; but said accounts payable when selected shall not exceed any one of the following amounts, whichever is the lower:

(a) The maximum sum of \$150,000.

(b) The amount by which the assets transferred and assigned as set forth in Schedules A-1, A-2, B, C and D, hereinbefore described, exceed the accrued liabilities and accrued taxes hereby assumed as set forth in Schedules F and G hereinafter referred to.

2. Assume and agree to pay certain accrued liabilities of the Construction Company and/or its Agent, Hotels Management and Securities Corporation, arising wholly and solely out of the operation of the "Properties" and accrued as of February 28, 1931, such accrued liabilities to be designated by the President of the Properties Company and to be particularly set forth on a schedule hereafter to be prepared and to be annexed hereto and marked Schedule F. (The parties hereto being unable now to affix said schedule to this agreement for the reason that the accountants
18 of the Company are unable at this time to report exactly thereon).

3. Assume and agree to pay real estate taxes accrued on the "Properties" and in the amounts as particularly set forth on a schedule hereunto annexed marked Schedule C.

4. The liabilities hereby assumed by the Properties Company shall in no event be less than an amount equal to the assets herein received from the Construction Company as per Schedules A-1, A-2, B, C and D.

III.

The parties hereto do mutually agree to terminate and cancel the Indenture of Lease made as of the 15th day of July, 1929, between the parties hereto and mentioned and described in the recitals hereof, effective as of the close of business February 28, 1931, and the Construction Company agrees to surrender and yield up to the Properties Company possession of the "Properties" and all its right, title and interest of the Construction Company under said lease of

July 15, 1929, and in and to all the real and personal property included in or described by said lease.

This agreement shall be binding upon and inure to the benefit of the parties hereto, their respective successors and assigns.

IN WITNESS WHEREOF, Wardman Real Estate Properties, Inc., has caused these presents to be signed in its corporate name by Thomas D. Carson, its President, attested by L. M. Hodges, its Secretary, and its corporate seal to be hereunto affixed and Wardman Realty and Construction Company has caused these presents to be signed by J. Reed Lane, its President, attested by George D. Johnson, its Assistant Secretary, and its corporate seal to be hereunto affixed, all as of the day and year first above written.

WARDMAN REAL ESTATE
PROPERTIES, INC.

By

Attest:

President.

.....

Secretary

19

WARDMAN REALTY AND
CONSTRUCTION COMPANY,

By

President.

Attest:

.....

Assistant Secretary

Summary of Schedules.

Credits:

Schedule A-1	Cash Transferred 2/27/31	\$ 46,608.12
Schedule A-2	Cash Receipts 2/27/31 and 2/28/31	14,782.89
Schedule B	Inventories	27,318.24
Schedule C	Deferred and Prepaid Items	68,022.70
Schedule D	Accounts Receiv- able	109,286.46
	Less reserve	25,312.69
		<u>\$240,702.40</u>

Charges:

Schedule E	Accounts Payable	119,549.85
Schedule F	Accrued Liabilities	73,498.87
Schedule G	Accrued Real Estate Taxes	47,653.68
		240,702.40

* * *

Schedule B.
Inventories
As at February 28, 1931.

Wardman Park Hotel:

Food		\$2,921.59
Beverage		543.73
Garage—Accessories	\$1,301.72	
Gasoline	852.14	
Oils and Grease	605.25	
Tires and Tubes	104.31	2,863.42

20	Brought forward		\$2,863.42	
	Drug Store—Cigars	284.60		
	Candy and			
	magazines	303.44		
	Soda	294.40		
	Drugs	16,153.58	17,036.02	\$23,364.76

Carlton Hotel:

Food		3,488.90	
Beverage		549.60	4,038.50

Stoneleigh Court:

Food		140.68	140.68
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Highlands:

Beverage		3.75	3.75
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Total Inventories as at close of business 2/28/31

27,547.09

* * *

*Schedule F.**Accrued Liabilities as at February 28, 1931.*

Accrued Salaries and Wages

Wardman Park Hotel	14,882.88	
Carlton	7,194.79	
Chastleton	1,737.42	
Apartments	6,795.85	
Mechanical	4,602.79	35,213.73

Accrued Light and Power

Wardman Park Hotel	725.39	
Chastleton	293.24	
Highlands	90.04	
Stoneleigh Court	92.24	
Cathedral Mansions	310.05	
Boulevard	233.60	
2700 Connecticut Avenue	62.00	1,806.56

Accrued Compensation Insurance

577.84

Accrued Gas

21 Wardman Park Hotel	47.67	
Carlton	108.51	156.18

Accrued Telephone

Carlton	1,816.85	
Chastleton	50.63	
Highlands	13.41	
Cathedral Mansions Center	96.31	1,977.20

Accrued Salaries and Wages Deferred

Wardman Park Hotel	13.82	
Carlton	15.00	
Highlands	10.50	39.32

Accrued Insurance—Not Yet Settled

Hancock Company	3,043.44
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Accrued Personal Property Taxes

Wardman Park Hotel	
From 7/1/29 thru 2/28/31	20,000.00

Carlton		
from 7/1/29 thru 2/28/31	6,950.00	
Chastleton		
from 7/1/28 thru 2/28/31	964.00	
Highlands		
from 7/1/28 thru 2/28/31	1,170.00	
Stoneleigh Court		
from 7/1/28 thru 2/28/31	1,258.00	
Cathedral Mansions		
from 7/1/28 thru 2/28/31	269.20	
Boulevard		
from 7/1/28 thru 2/28/31	51.00	
2700 Conn. Avenue		
from 7/1/30 thru 2/28/31	22.40	30,684.60
Total accrued liabilities		<u>\$73,498.87</u>

VI. Pursuant to the aforesaid agreement between the Construction Company and the Properties Company, the possession, operation and control of the properties was surrendered by the Construction Company to the Properties Company as of February 28, 1931. The assets which the Construction Company agreed to assign to the Properties Company, were in fact assigned to the Properties Company, and the Properties Company proceeded to pay and did pay all of the obligations which it had assumed under said contract excepting claims aggregating \$924.00 which were disputed and the personal property taxes then believed to be claimed by the District of Columbia from the Construction Company which were afterwards asserted in larger amounts as direct preferred claims against the Properties Company and are now disputed and in litigation herein. The Construction Company had other assets not assigned to the Properties Company.

VII. In addition to the inventories referred to in Schedule B of the cancellation agreement between the Construction Company and the Properties Company, taken over by the Properties Company pursuant thereto, there were coal, hardware, soaps, cleaning materials and other goods, wares and merchandise on hand in the eleven apartment houses and hotels on February 27, 1931, which were taken over by the Properties Company without

(Hence, ordinary trade accounts of construction Co. were paid)

adjustment between the two companies. The same procedure had been followed between the two companies on July 15, 1929, at the time the lease was entered into, at which time the Construction Company took over similar materials from the Properties Company without adjustment.

VIII. From March 1, 1931, until July 14, 1931, the properties were operated by the Properties Company when, default having been made by the Properties Company under the indenture securing its first and refunding mortgage bonds, the District Court of the United States for the District of Columbia, in Equity Cause No. 53117, appointed the appellees Julius I. Peyser and Joseph P. Tumulty and Thomas D. Carson, since resigned, as receivers of all of the mortgaged assets of the Properties Company. On the day of July, 1931, in Equity Cause No. 53180, being a general creditors suit, the same receivers were appointed receivers of all of the unmortgaged assets of the Properties Company in the District of Columbia. The receivers now have on hand in this Equity receivership No. 53180, the sum of approximately \$197,917.30.

IX. As of September 1, 1928, the Construction Company had issued \$2,500,000 senior debenture bonds and \$2,400,000 junior debenture bonds. At the time of the cancellation of said lease, the Construction Company had paid all interest then due on its debentures.

X. As of September 1, 1928, the Properties Company had issued \$11,350,000 of first and refunding mortgage bonds, of which \$10,963,000 were outstanding at the time of the cancellation of the lease. It had also issued a \$2,500,000 general mortgage bond to the Construction Company, junior to the first and refunding bonds, which general mortgage bond had been pledged by the Construction Company as collateral for its debentures. There was no default in interest under said general mortgage bond at the time of the cancellation of the lease.

XI. A sale of the properties at the suit of the trustee in Equity Cause No. 53117 was decreed by the District Court of the United States for the District of Columbia on October 14, 1931, and the sale was made October 21, 1932. The appellee Washington Properties, Inc., became the final purchaser, and title was conveyed to that corporation.

See substitute #XII.

~~XII. On the 2nd day of January, 1934, a deficiency judgment, in Equity Cause No. 53117, was awarded in the District Court of the United States for the District of Columbia to appellee Washington Properties, Inc., in the sum of \$10,470,039.09. Said Washington Properties, Inc., through the reorganization plan pursuant to which it purchased the properties, also acquired the general mortgage bond of the Properties Company in the amount of \$2,500,000, for which claim had been filed and allowed in these proceedings, and also acquired \$2,080,500. of the aforesaid senior debentures of the Construction Company.~~

XIII. On April 8, 1931, the Properties Company, pursuant to resolution of its board of directors, set up a reserve on its books against the account of the Construction Company in the amount of \$654,000. after which its account against the Construction Company was carried on its books at the nominal figure of \$1.00. This same practice was followed by the receivers in their reports filed with the court.

XIV. By order of April 19, 1933, the District Court of the United States for the District of Columbia referred said Equity Causes 53117 and 53180 to A. Leftwich Sinclair as Special Master, and directed all persons having claims or demands against the Properties Company or the receivers or against any property in the hands of the receivers to file the same with the Special Master on or before June 30, 1933, as follows:

24 *Order Limiting Time for Presentation of Claims, Authorizing Provisional Allowance by Receivers, and Referring Cause to Special Master*

These causes came on to be heard upon the report of Joseph P. Tumulty and Julius I. Peyser, receivers herein, filed on the 6th day of April, 1933, and it appearing to the court that the matters involved in this cause are of a nature requiring the detailed examination of claims and accounts, and that other exceptional conditions require it, it is by the court this 19th day of April, 1933, ORDERED as follows, viz:

1. A. Leftwich Sinclair, auditor of this court, is hereby appointed special master in this cause with the usual powers exercised by special masters in like cases under the rules of this court and under the equity rules of the United States

Supreme Court having relation thereto, and under such subsequent orders as this court may enter herein.

2. The special master is authorized and directed to state the account of the receivers filed herein on the 6th day of April, 1933, and report his findings thereon to the court.

25 3. The special master is authorized and directed to take testimony, make findings of fact, adopt conclusions of law and report to the court respecting the ownership of the items referred to in the "memo account" of the receivers referred to in their said report filed herein on the 6th day of April, 1933.

4. All persons, firms or corporations having claims or demands against the defendant, Wardman Real Estate Properties, Inc., or the receivers herein, or against any property in the hands of the receivers, are required on or before the 30th day of June, 1933, under penalty of thereafter having said claims disallowed in the discretion of the court, to file the same with the special master, sending copy thereof to the receivers herein, at the offices of their counsel, Messrs. Douglas, Obear & Douglas, 822 Southern Building, Washington, D. C., which said claims or demands shall be supported by affidavit and shall set out the amount and nature of any security or lien held by the claimant or to which the claimant is entitled, and also any claims of preference in payment out of the assets in the hands of the receivers in this cause, or to any other creditors of the said defendant, Wardman Real Estate Properties, Inc.

5. The said Joseph P. Tumulty and Julius I. Peyser, receivers, shall as soon as they conveniently can after the 19th day of April, 1933, publish each week for two successive calendar weeks in a newspaper published and having general circulation in the District of Columbia and in the Washington Law Reporter, notice to all persons, firms and corporations interested in the subject matter of this order of the substance of the order having relation to the filing of claims, and shall also give not less than twenty days notice by mail to all creditors and claimants of whose names and addresses they may be informed.

6. The receivers are hereby authorized provisionally to allow any claims so filed. They are hereby further authorized provisionally to compromise and liquidate any such claim. Such provisional allowance, compromise or

26 liquidation shall not be construed to change the burden of proof in the event of objection to the claim as hereinafter provided for. The receivers shall from time to time file with the special master a report of all claims thus provisionally allowed or provisionally compromised and liquidated by them. Upon the filing of such report the receivers shall give notice of filing thereof by mail to the attorneys of record in these causes. Any party to this suit or any person interested in the distribution of the proceeds of property in the hands of the receivers may within twenty days after the mailing of the notice of such report object to any such claim by filing a written notice of objection with the special master, sending copy thereof to the receivers at the offices of their counsel, as aforesaid.

7. No such allowance or provisional compromise and liquidation of any such claim by the receivers shall be deemed to make the claim so liquidated an obligation of the receivers not give authority to the receivers to make payment of the amount thereof, but all such claims shall be reserved for future and final disposition by this court.

8. All claims and demands now or which may hereafter be filed with the special master which are not provisionally allowed by the receivers or provisionally compromised and liquidated by the receivers herein, or which are objected to by the filing of objections as aforesaid, shall be considered referred to the special master, who shall take testimony with reference thereto and report such testimony to this court, together with his findings of fact and conclusions of law thereon.

9. The court reserves the right at any time to fix a reasonable time within which all claims referred to the special master shall finally be proved before said special master.

10. Nothing contained in this order shall adversely affect, or bar, the rights of any one having a claim against the Wardman Real Estate Properties, Inc., or to the funds in the hands of the receivers, which is now in process of being determined in any suit pending in this court, including the right, if any, to a deficiency decree in Equity Cause No. 53,117 and which has not been finally adjudicated by judgment or decree prior to the expiration of

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the time herein limited for filing claims. The court hereby reserves the right with respect to all claimants, both tort and contract, both in *rem* and in *personam*, who either have brought suit heretofore or who may hereafter elect to bring suit, to require at any time that such claimants, irrespective of the status of their suit, shall by a day certain prove their claims before the special master in order to permit the termination of this receivership proceeding.

11. The special master shall make seasonable reports from time to time on the several separate matters and things herein referred to him.

12. Any party or claimant may apply for modification of any of the terms of this order upon cause shown at any time upon notice and all matters not hereby disposed of or determined are reserved for future adjudication.

/s/ JAMES M. PROCTOR
Justice.

28 XV. On July 31, 1931, the Circuit Court of the City of Baltimore adjudicated the Wardman Realty and Construction Company insolvent, and appointed the appellant, Edwin H. Brownley, Statutory Receiver of this company, and on the 9th day of September, 1931, with leave of the Court, the appellant as Statutory Receiver, filed an intervening petition in the said causes, asserting the right to the possession of certain of the unmortgaged assets of the said Properties Company, as hereinafter set out in the claim of Edwin H. Brownley, Statutory Receiver, filed with the Special Master.

XVI. Among the claims filed with the Special Master was one filed by the appellant Edwin H. Brownley as statutory receiver of the Construction Company, which claim was as follows:

29 *Claim or Demand of Edwin H. Brownley, Statutory Receiver, Wardman Realty and Construction Co., Against Receivers, Wardman Real Estate Properties, Inc., and Moneys and Other Property in the Hands of Said Receivers.*

The claimant, Edwin H. Brownley, was on the 31st day of July, 1931, appointed by order of the Circuit Court of Baltimore City, Maryland, and duly qualified, Statutory

Receiver of the Wardman Realty and Construction Company, a Maryland corporation, hereinafter called the Construction Company. The said Construction Company was the sole stockholder of the Wardman Real Estate Properties, Inc., hereinafter called the Properties Company, and the claim or demand of the said Construction Company against the said receivers, and the moneys and other property in the hands of the said receivers arose as follows:

1. On March 7, 1931, the identical officers and directors of the said Properties Company and the said Construction Company, acting for both corporations, unlawfully transferred and removed from the assets of the Construction Company practically the entire assets of the Company embracing goods, wares, merchandise, cash and accounts receivable, aggregating \$266,015.09, besides coal, hardware and other goods, wares and merchandise not accounted for, and unlawfully transferred the same to the Properties Company in fraud of the creditors of the said Construction Company.

II. The general mortgage executed by the Properties Company securing debentures of the Construction Company expressly excepted and excluded from the lien and operation of that mortgage of the aforesaid assets in the following language:

“There is, however, expressly excepted and excluded from the lien and operation of this mortgage, any cash on hand or in bank, stock in trade held for resale, securities, bills, notes, accounts receivable and other choses in action, not expressly described or mentioned herein and specifically pledged hereunder or covenanted so to be.”

3. When the Properties Company entered into a lease with the Construction Company for the operation of the

30 Wardman properties, the Construction Company entered into a contract with the United Realities, Inc.

for the management of these properties, and in said management contract it was expressly provided that a revolving fund of \$200,000.00 should be provided, which, together with the operating revenues, should be kept for the payment of all operating, maintenance and capital expenditures, as follows:

“For the purpose of providing adequate working capital for the proper administration of the properties to be man-

aged by the United Company, Construction Company, shall, on or before the date when the properties are to be turned over to the United Company, deposit with a Washington or Baltimore bank or banks, trust company or trust companies, for the use of the United Company as a revolving fund in connection with the operation of said properties the sum of Two hundred thousand dollars (\$200,000.). The said deposit together with the operating revenues herein-after mentioned (herein called special account) shall be kept separate and apart from any moneys and other funds of the United Company and shall be the property of the Construction Company but subject to the use of the United Company as herein provided. The special account shall be opened in the name of United Realities, Inc., Agent, and the funds in said special account shall be subject to withdrawal from said special account upon, and only upon, the check of the United Realities, Inc., Agent signed by such officer or executive as it may designate, countersigned in each case by such person or persons as the Construction Company may from time to time designate. The United Company shall also collect and receive all moneys from the operation of the properties and shall deposit the same in the said special account. All of said funds in said special account shall be available for use of the United Company in the payment of all operating, maintenance and capital expenditures or other disbursements provided for herein during the life of this agreement. It is understood and agreed, however, that the United Company shall not authorize or make any capital expenditure on the properties at any one time (except emergency expenditures necessary to be made immediately for the preservation of any of the properties) in excess of one Thousand Dollars (\$1,000) except with the written consent first obtained of the Board of Directors of Construction Company or the agent of the Board duly authorized for that purpose. Subject to the limitations herein mentioned, United Company shall have full power to make all disbursements out of said special account which it may deem necessary or advisable in the proper performance of this agreement."

4. The funded obligations of the Construction Company were \$2,500,000. 8½% gold debentures secured by the stock of the Properties Company owned by the Construction

Company, and by the said general mortgage of \$2,500,000.
and \$2,400,000. 6% gold debentures, the latter being
31 subject to the prior pledge of the stock and general
mortgage bond given to secure the first debentures.

In the indentures are covenants on the part of the Company not to incur indebtedness beyond sixty days, and a further covenant to maintain, operate and expend funds for the maintenance and operation, and to pay all obligations incurred therefor, so that no lien might exist prior to the debenture notes, as follows:

“Sec. 6. That it will duly pay and discharge, as the same shall become due and payable, all taxes, assessments and governmental and other charges lawfully levied and imposed upon the trust estate and upon the franchises, properties, earnings and business of the Company, and also all taxes, assessments and governmental charges lawfully imposed upon the lien or interest of the Trustee in respect of the trust estate and the income and profits thereof, as well as all lawful claims for rents, labor, material and supplies, which if unpaid might by law become a lien or charge upon any of the properties of the Company; provided, however, that nothing contained in this section shall require the Company to pay any such tax, assessment, claim or charge so long as the Company in good faith shall contest the validity thereof, unless thereby, in the opinion of the Trustee or of counsel, the rights and security of the holders of the debentures shall be materially endangered.”

“Sec. 10. That it will not extend, or enter into any agreement with any one or more of its creditors whereby it will consent to the extension of, more than fifty per cent. (50%) of its current indebtedness at any one time outstanding for a period or periods which, together with prior extensions, shall be in excess of sixty (60) days.”

5. The claimant asserts that the cash, accounts receivable, inventories, choses in action belonging to the Construction Company on the said March 7, 1931, were assets for the payment of its current debts for the maintenance and operation of said properties, and that the creditors of the Construction Company, especially those who supplied services, goods, wares and merchandise in the normal course of business for maintenance and operation thereof, are entitled to the whole of said assets.

6. When the said identical officers and directors of the said corporations agreed to transfer all of the assets of the Construction Company to the Properties Company, they entered upon the minute books of the said Construction Company the following:

Summary of Schedules Annexed

Credits:

Schedule A-1	Cash Transferred 2/27/31	\$48,608.12
Schedule A-2	Cash Receipts 2/27/31 and 2/28/31	14,782.59
Schedule B	Inventories	27,318.24
Schedule C	Deferred and Prepaid Items	68,022.70
Schedule D	Accounts Receivable	109,285.44
	less reserve	25,312.69
		\$240,702.40

Charges:

Schedule E	Accounts Payable	119,549.85
Schedule F	Accrued Liabilities	73,498.87
Schedule G	Accrued Real Estate Taxes	47,653.68
		\$240,702.40

Claimant is not informed as to what accounts receivable by the Construction Company were collected by the Properties Company or its receivers, nor what accounts payable by the said Construction Company were settled and discharged by the said Properties Company, but there are many outstanding and unsettled bills due by the said Construction Company, none of which can be paid by the claimant as receiver of said Company because all of its assets were unlawfully removed and taken by the said Properties Company.

7. The claimant asserts that embraced within the accrued liabilities in Schedule F, as set out in the above summary, is the sum of \$30,684.60, alleged personal property taxes accrued since July 1, 1928. This item has not been paid by the said Properties Company or by the said receivers, is not collectible, is an improper and fictitious charge, and in

any event, is an attempt on the part of the Properties Company to prefer itself as a creditor of its parent corporation over the other creditors of said Construction Company. Embraced in Schedule G of the above summary is an item of accrued real estate taxes in the sum of \$47,653.68. This was a primary debt of the said Properties Company, and in charging it against the said Construction Company's assets, which the Properties Company unlawfully took, the said Properties Company unlawfully attempted to prefer itself to the other creditors of its parent corporation, the said Construction Company. The inventories aggregating \$27,318.24, listed in Schedule B among the assets of the Construction Company which were unlawfully removed and taken over by the said Properties Company, do not embrace any of the coal, hardware, soaps, cleaning materials and other goods, wares and merchandise on hand on February 27, 1931 in the eleven apartment houses and hotels, but the whole of the said inventories were unlawfully transferred in bulk by the parent corporation to its wholly owned subsidiary, the Properties Company, in fraud of the creditors of the Construction Company.

8. The claimant asserts that the chattel mortgage upon the furniture and fixtures of the Hay Adams House is the property of the Construction Company, and has never been assigned by said Company in any manner to its wholly owned subsidiary, the Properties Company, and said chattel mortgage should be delivered to the receiver of the said Construction Company for the protection of its creditors.

9. That within four months from the attempted transfer by the Construction Company, then wholly insolvent, to its wholly owned subsidiary, the Properties Company, of all of its assets, the said Construction Company caused to be paid out of its funds many thousands of dollars in payment for household furniture, plumbing supplies, steam mains and boilers and other equipment of the said apartment houses and hotels wholly owned by the said subsidiary corporation, and in fraud of the creditors of the Construction Company, said payments aggregating more than
34 \$25,000., for which account should be made to the receiver of the said Construction Company for the protection of its creditors.

10. The claimant therefore asserts that as receiver of the said Construction Company, he is entitled to be paid out of the cash in the hands of the receivers of the said Properties Company, at least the following items:

Unpaid personal property taxes	\$30,684.60
Accrued real estate taxes	47,653.68
Inventories	27,318.24
(And in addition the value of the coal, hardware and other goods, wares and merchandise on hand at the time of the unlawful transfer and removal in bulk of the said assets to the said Properties Company)	
Lien on the furniture and equipment at the Hay Adams House	56,000.00
Unlawful payments on the Properties Company's properties within four months	25,000.00
	\$186,656.52

Subject to increase by a proper accounting of the accounts receivable and accounts payable.

/s/ EDWIN H. BROWNLEY
*Edwin H. Brownley, Statutory
 Receiver, Wardman Realty and
 Construction Company.*

/s/ CARLIN and CARLIN
 /s/ LESLIE C. GARNETT
Attorneys for Receiver.

35 *Affidavit of Edwin H. Brownley*

DISTRICT OF COLUMBIA, *to-wit:*

Edwin H. Brownley, being first duly sworn, deposes and says that he is the Statutory Receiver of the Wardman Realty and Construction Company under decree of the Circuit Court of Baltimore City; that the foregoing claim or demand against the Receivers of the Wardman Real Estate Properties, Inc., and the moneys and other property in the hands of the said Receivers is true, and the amounts therein stated are correct to the best of his knowledge and belief.

/s/ EDWIN H. BROWNLEY

Subscribed and sworn to before me this 6th day of May, 1933.

/s/ IDA E. PARKER
Notary Public.

My commission expires the 1st day of March, 1937.

XVII. Hearing on this claim was had before the Special Master September 21, 1933 and thereafter, and the Special Master on the 9th day of April, 1936, submitted his final report rejecting *in toto* the claim of the appellant. The following is an extract of the Special Master's finding:

Claim of Edwin H. Brownley, as Statutory Receiver of Wardman Realty and Construction Company.

23. The claim of Edwin H. Brownley, as statutory receiver of the Wardman Realty and Construction Company, filed with the Special Master on May 9, 1933, is in the amount of \$186,656.52. This claim may properly be
36 divided into the following items:

(1) Assets taken over by Wardman Real Estate Properties, Inc., from Wardman Realty and Construction Company under agreement of March 7, 1931, \$105,636.52.

(2) Alleged unlawful payments on properties belonging to Wardman Real Estate Properties, Inc., within four months of the receivership, \$25,000.00; and

(3) Alleged lien on furniture and equipment at the Hay-Adams House, \$56,000.00.

These items will be considered in the order in which they have been stated.

(1) Testimony was given in support of this claim by J. Reed Lane, who prior to the time Wardman Realty and Construction Company released its lease of the Wardman properties to Wardman Real Estate Properties, Inc., was president of both companies, (See Record of hearings, Vol. 1, pp. 106-138). The claimant offered in evidence a lease between Wardman Real Estate Properties, Inc., and Wardman Realty and Construction Company, dated as of July 15, 1929, whereby the Construction Company leased from Wardman Real Estate Properties, Inc., the properties owned by the latter, and agreed to pay, as rent for said properties, all interest which became due on the bonds of Wardman Real Estate Properties, Inc., secured on said

properties, and all real estate taxes thereon. (See Record of hearings, Vol. 1, p. 115). It appears that on February 28, 1931, Wardman Realty and Construction Company was in default in the payment of the rentals specified in said lease, in a sum slightly in excess of \$654,000.00, (See Record of hearings, Vol. 1, pp. 116), and that on March 7, 1931, an agreement was entered into between Wardman Real Estate Properties, Inc., and Wardman Realty and Construction Company, under which said lease was terminated and cancelled as of the close of business February 28, 1931, and the operation of said properties taken back into the hands of Wardman Real Estate Properties, Inc. At that time it was agreed between the two companies that the Realty and Construction Company would transfer to Wardman Real Estate Properties, Inc., approximately \$240,000.00 worth of assets, and Wardman Real Estate Properties, Inc., in turn assumed and agreed to pay debts of the Realty and Construction Company in an equal amount. Among the debts assumed by Wardman Real Estate Properties, Inc., (See Record of hearings, Vol. 1, pp. 117-125), were approximately \$119,000.00 worth of accounts payable to the Realty and Construction Company, representing all its ordinary trade accounts, and \$73,000.00 worth of accrued liabilities, which included personal taxes and \$37,000.00 real estate taxes. It appears that the indebtedness of the Realty and Construction Company to Wardman Real Estate Properties, Inc., of \$654,000.00 was not affected by said agreement; but that the account at a later date, was arbitrarily written down on the books of Wardman Real Estate Properties, Inc., to \$1.00. (See Record of hearings, Vol. 1, pp. 143-146).

It appears that, in addition to the above-mentioned assets of Realty and Construction Company taken over by Wardman Real Estate Properties, Inc., under said agreement, there were certain consumable stock used in the operation of the properties, such as coal, hardware and other goods, wares and merchandise, then on hand, estimated by the witness Lane to be of the value of between \$20,000.00 and \$25,000.00, (See Record of hearings, Vol. 1, p. 112); but valued by the witness Lloyd at not more than \$5,000.00. (See Record of hearings, Vol. 1, p. 139).

✓ correction by Lesh

38 (2) With respect to the alleged unlawful payments on properties belonging to Wardman Real Estate Properties, Inc., it was claimed by the Realty and Construction Company, the sole stockholder of Wardman Real Estate Properties, Inc., that within four months of the date of said agreement of March 7, 1931, it made payments aggregating approximately \$25,000.00 out of its funds for household furniture, plumbing supplies, steam mains and boilers and other equipment on the properties owned by Wardman Real Estate Properties, Inc., "*in fraud of the creditors of the Construction Company.*" But no definite testimony was offered in support of this claim; while an examination of the *lease* between the two companies shows that the Realty and Construction Company was obligated to make such payments.

The Realty and Construction Company apparently received full present consideration for the assets transferred by it to Wardman Real Estate Properties, Inc., under the agreement of March 7, 1931. For the evidence shows that Wardman Real Estate Properties, Inc., under said agreement, assumed obligations of the Realty and Construction Company *in an amount equal to the value of such assets*; and that when the agreement was made it was believed to be fair and for the best interests of all concerned. (See Record of hearings, vol. 1, pp. 124, 125).

It is to be noted, that Wardman Realty and Construction Company was not in bankruptcy at the time of the transfer of its assets under the agreement of March 7, 1931; and that in the absence of a showing of bankruptcy occurring within four months, the transfer could at most have been regarded as a preferential payment by the Realty and Construction Company to one of its principal creditors.

It seems to the Special Master, that to permit Wardman Realty and Construction Company to recover the sums claimed, under the circumstances disclosed, would be
39 inequitable and unfair to the creditors of Wardman Real Estate Properties, Inc., and contrary to law.

(3) As to the alleged lien of Wardman Realty and Construction Company on furniture and equipment at the Hay-Adams House, the claimant asserts "that the chattel mortgage upon the furniture and fixtures of the Hay-Adams House is the property of the Construction Company and

has never been assigned by said Company, in any manner to its wholly owned subsidiary, the Properties Company, and said chattel mortgage should be delivered to the receiver of the Construction Company for the protection of its creditors."

The showing made in the testimony is insufficient, in the opinion of the Special Master, to sustain this contention.

While it appears that Wardman Realty and Construction Company at one time owned the Hay-Adams chattel note, the testimony shows that the Company pledged the note as collateral security for an obligation of \$550,000.00, and that the Hay-Adams collateral was thereafter sold to Hotels Management and Securities Corporation. (See Record of hearings, Vol. 1, pp. 122-127). It appears from a report filed with the Court by the Receivers in these causes, on December 31, 1931, that the Hay-Adams collateral was then pledged with them as collateral for a note of Hotels Management and Securities Corporation, dated June 29, 1931, in the principal sum of \$50,000.00; and that upon the Receivers' recommendation, the Court, by order of December 4, 1931, authorized the Receivers to sell said collateral at public auction because of the default of Hotels Management and Securities Corporation in the payment of its said note, and to bid for said Hay-Adams collateral the sum of \$50,000.00. The testimony shows that said collateral was sold by the Receivers at public auction, pursuant to said order and that at said sale, the Receivers purchased
40 the notes secured by the chattel trust on the Hay-Adams furniture, for the sum of \$50,000.00. (See record of hearings, Vol. 1, p. 147).

24. On the whole evidence, the Special Master finds that the claim of said Edwin H. Brownley, as statutory receiver of Wardman Realty and Construction Company, should be disallowed *in toto*.

XVIII. It is stipulated between the parties to this appeal that the statements of fact contained in the report of the Special Master contain a correct digest of the testimony adduced before him on the subject matter, except in so far, if at all, as they may be inconsistent with the agreed statement of facts heretofore found herein.

XIX. The appellant excepted to the findings of the Special Master as follows:

Exceptions to the Report of A. Leftwich Sinclair, Auditor of the Supreme Court of the District of Columbia, Special Master.

Comes now Edwin H. Brownley, Statutory Receiver of the Wardman Realty and Construction Company, and excepts to the report of the Special Master filed herein on April 9, 1936, as follows:

1. The said Special Master erred in denying the claim of the said exceptant in the sum of \$186,656.52.

2. The Special Master erred in not holding and deciding that the cash, accounts receivable, inventories and choses in action belonging to the Wardman Realty and Construction Company on March 7, 1931, were assets of the said Company for the payment of its current debts for the maintenance and operation of its properties, and that the creditors of said Company, especially those who supplied services, goods, wares and merchandise in the normal course of business for the maintenance and operation of said properties, were entitled to the whole of said assets.

3. The Special Master erred in not holding and deciding that the same directors who were directors of the Wardman Realty and Construction Company, the sole stockholder of the Wardman Real Estate Properties, Inc., and who were also directors of the Wardman Real Estate Properties, Inc., on March 7, 1931, acting for both corporations, unlawfully transferred and removed from the assets of the Construction Company practically the entire assets of the last named Company, embracing goods, wares, merchandise, cash and accounts receivable, aggregating \$265,015.09, besides other personal property not accounted for, and unlawfully transferred the same to the said Properties Company in fraud of the creditors of the said Construction Company.

4. That the said Special Master erred in upholding the action of the same directors acting for both companies in preferring as creditors the Wardman Real Estate Properties, Inc., the wholly owned subsidiary of the said Wardman Realty and Construction Company, the same being practically one corporation.

5. The Special Master erred in not holding and deciding that the claimant was entitled as Receiver of the Wardman

Realty and Construction Company, to be paid out of the cash in the hands of the Receivers of the said Properties Company, the following items improperly charged by the said Receivers of the Wardman Real Estate Properties, Inc., against the said Wardman Realty and Construction Company, to wit:

Unpaid personal property taxes	\$30,684.60
Accrued real estate taxes	47,653.68
Inventories	27,318.24

(And in addition the value of the coal, hardware and other goods, wares and merchandise on hand at the time of the unlawful transfer and removal in bulk of the said assets to the said Properties Company)

6. The said Special Master erred in not holding and deciding that the action of the identical directors of the two Companies, when the Wardman Realty and Construction Company was wholly insolvent in paying out of its funds to the detriment of those creditors who supplied services, goods, wares and merchandise in the normal course
42 of business for the maintenance and operation of the said Properties Company, was not a fraud on such creditors of said Construction Company, and an accounting should be made thereof to the Receiver of the Construction Company for the protection of its creditors.

7. The said Special Master erred in holding and deciding that the agreement by which the Wardman Real Estate Properties, Inc., acquired all of the assets of the Wardman Realty and Construction Company was fair and to the best interests of the creditors of the Construction Company, since the same amounted to a preference of the Wardman Real Estate Properties, Inc., as a creditor of its wholly owned subsidiary.

8. The Special Master erred in holding and deciding that the writing off of any supposed indebtedness for rent between the two Corporations identically controlled, and in legal effect identical Corporations, should not enure to the benefit of the creditors of the Wardman Realty and Construction Company who dealt with said Corporation on the strength of its assets.

9. For these and other just grounds of exception the exceptant prays that the Report of the said Special Master, paragraph 23 denying the claim of the exceptant, the Statutory Receiver of the Wardman Realty and Construction Company, be not confirmed.

EDWIN H. BROWNLEY, *Statutory Receiver*,
WARDMAN REALTY & CONSTRUCTION
COMPANY.

By Counsel.

C. C. CARLIN,
LESLIE C. GARNETT,
Attorneys for Edwin H. Brownley,
Statutory Receiver, Wardman
Realty & Construction Company.

43 XX. The District Court filed a memorandum opinion overruling the appellant's exceptions, and ratified and confirmed the report of the Special Master, as follows:

Memorandum Overruling Exceptions and Confirming Report of Special Master in Part, and Referring Report to Special Master for further Findings and Conclusions.

This matter is now before the court on the exceptions to the second and final report of the Special Master, Leftwich Sinclair, filed herein on the 9th day of April, 1936.

The exceptions, filed by E. S. Poston and Company, Walter M. Ballard Company, Security Savings and Commercial Bank, Edwin H. Brownley, as Receiver for Wardman Realty and Construction Company and Henry P. Blair and Michael M. Doyle, trustees in bankruptcy for Swartzell, Rheem and Hensey Company, are severally overruled and the report of the Special Master with respect to each of such claims is ratified and confirmed.

The Special Master in said report allowed the claims of the District of Columbia for taxes in the sum of \$52,936.20 and for water rent in the sum of \$774.48.

The Washington Properties, Inc. excepts to the allowance of the claim for taxes and also to the claim for water rent.

Julius I. Peyser and Joseph P. Tumulty, receivers, except to the allowance of the claim of the District for taxes.

The District of Columbia excepts to the report in so far as it allows only the sum of \$52,936.20 for taxes, and fails to allow in addition thereto the claimed penalties.

The exceptions of Washington Properties, Inc. to the allowance of the claim of the District of Columbia for \$77.48 on account of water rent will be overruled and the report ratified and confirmed.

It appears from the report that the amount allowed
44 the District of Columbia for taxes was the amount of tax due without the addition of any penalty on account of delinquency, and that the item of penalty was not considered by the Special Master, although the District made claim for penalties.

The report will be referred back to the Special Master and he will be ordered to further consider the claim of the District of Columbia and report to the court within ten days further and additional findings and conclusions with respect to said claim.

Pending such further report, the exceptions referring to such claim will be held under advisement, provided that additional exceptions may be filed to such further findings and conclusions within ten days by the Washington Properties, Inc., Julius I. Peyser and Joseph P. Tumulty, as receivers, and the District of Columbia, if counsel are so advised.

Counsel will please prepare proper order.

/s/ O. R. LUHRING
Justice.

February 15, 1937.

XXI. Order of February 18, 1937:

Order Overruling Certain Exceptions and Confirming Report of Special Master and Referring Report back to Special Master for Further Findings.

This cause came on to be heard on the exceptions filed by the parties hereinafter named to the second and final report of A. Leftwich Sinclair, Special Master, filed herein April 9, 1936, and was argued by counsel for the said parties, respectively, and upon consideration thereof, it is by the Court this 18th day of February, 1937.

45 ORDERED that the exceptions filed to said report by E. S. Poston & Co., by Walter M. Ballard Co., by

Security Savings & Commercial Bank, by Edwin H. Brownley, as receiver for Wardman Realty and Construction Company, and by Henry P. Blair and Michael M. Doyle, trustees in bankruptcy of Swartzel, Rheem & Hensey Company, as to their several claims, be and the same are hereby severally overruled, and the report of the Special Master with respect to each of such claims is hereby ratified and confirmed; and

FURTHER ORDERED that the exceptions filed to said report by Washington Properties, Inc., to the allowance of the claim of the District of Columbia for \$774.48 on account of water rent, be and the same are hereby overruled, and the report of the Special Master with respect to such claim is hereby ratified and confirmed; and

FURTHER ORDERED that said report be and the same is hereby referred back to the Special Master, and said Special Master be and he is hereby ordered to consider further the claim of the District of Columbia for penalties for delinquency in the payment of the personal property taxes reported by said Special Master to be due, and to report to the Court within ten days further additional findings of fact and conclusions of law with respect to said claim, and that said Special Master may proceed upon this reference in his discretion without additional testimony, hearings or notice, except that notice of any hearing to be held before said Special Master and of the filing of his further report shall be given to counsel for the parties whose exceptions concerning said claim are hereinafter dealt with; and

FURTHER ORDERED that the exceptions filed by Washington Properties, Inc., and by Julius I. Peyser and Joseph P. Tumulty, receivers herein, to the allowance by the Special Master in his said report of the claim
46 of the District of Columbia for personal property taxes in the sum of \$52,956.20, and the exceptions by the District of Columbia to the said report in so far as it fails to allow in addition to said amount for personal property taxes the penalties claimed by the District of Columbia to have accrued thereon, be and the same are hereby held under advisement by the Court, provided that additional exceptions may be filed to such further findings and

conclusions as the Special Master may report with regard to said claim within ten days after the Special Master shall file his report, by Washington Properties, Inc., Julius I. Peyser and Joseph P. Tumulty, as receivers herein, and the District of Columbia, if said parties shall be so advised.

/s/ O. R. LUHRING
Justice.

From the foregoing an appeal noted in open Court by Counsel for The Walter M. Ballard Co. and Security Savings & Commercial Bank. Cost bond fixed at \$100.00 or cash deposit of \$50.00 in lieu thereof.

/s/ O. R. LUHRING,
Justice.

Feb'y. 18th—1937

From the foregoing an appeal is noted in open Court for Edwin H. Brownley, Receiver for Wardman Realty & Construction Co. Cost bond fixed at \$100. or cash deposit of \$50. in lieu thereof.

/s/ O. R. LUHRING,
Justice.

Feb'y. 18th—1937

Memorandum

MARCH 8, 1937.

\$50 cash deposited in lieu of Bond on Appeal, by Leslie C. Garnett.

47

Stipulation of Counsel.

It is hereby stipulated that the foregoing agreed statement constitutes the pleadings and motions filed, made and submitted by either party prior to the decision of this cause below, and is the statement of the case showing questions of fact and law presented, and the rulings and decisions thereon, and sets forth only so much of the facts alleged and and proved or admitted or sought to be proved, as either or all of the parties deem essential to a decision of such questions on appeal. This statement is prepared and

signed in accordance with the provisions of Rule 5 of the United States Court of Appeals, and is herewith presented to the trial Justice for his approval.

LESLIE C GARNETT

Attorney for Edwin H. Brownley, Statutory Receiver, Wardman Realty & Construction Company.

April, 1937.

DOUGLAS O'BEAR MORGAN and CAMPBELL

Attorneys for Julius I. Peyser and Joseph P. Tumulty, Receivers, Wardman Real Estate Properties, Inc.

By EDMUND D. CAMPBELL

PAUL E. LESH,

Attorney for Washington Properties, Inc.

I, Oscar R. Luhring, Justice who presided at the hearing of the above entitled cause, approve the foregoing statement of the case as evidenced by my signature in duplicate, one copy to be filed with the Clerk of this Court and the other with the Clerk of the United States Court of Appeals for the District of Columbia.

O R LUHRING

Justice.

May 3rd, 1937.

48 District Court of the United States for the
District of Columbia

Equity Nos. 53117 and 53180

CENTRAL HANOVER BANK & TRUST Co., a body corporate, and
FRANK WOLFE, trustee, et al, *plaintiffs*

vs.

WARDMAN REAL ESTATE PROPERTIES, INC, and RANDOLPH P.
COMPTON, et al, *defendants*

I, Charles E. Stewart, Clerk of The District Court of the United States for the District of Columbia, do hereby certify the annexed to be true and correct copies of the originals

as (they) appear of record in Clerk's Office of said Court in the above-entitled cause.

IN TESTIMONY WHEREOF, I hereunto subscribe my name and affix the seal of said Court, at the City of Washington, this 4th day of May, 1937

C. E. STEWART,
Clerk.

(Seal)

49 *Order Overruling Certain Exceptions and Confirming Report of Special Master and Referring Report Back to Special Master for Further Findings.*

This cause came on to be heard on the exceptions filed by the parties hereinafter named to the second and final report of A. Leftwich Sinclair, Special Master, filed herein April 9, 1936, and was argued by counsel for the said parties, respectively, and upon consideration thereof, it is by the Court the 18th day of February, 1937,

ORDERED that the exceptions filed to said report by E. S. Poston & Co., by Walter M. Ballard Co., by Security Savings & Commercial Bank, by Edwin H. Brownley, as receiver for Wardman Realty and Construction Company, and by Henry P. Blair and Michael M. Doyle, trustees in bankruptcy of Swartzell, Rheem & Hensey Company, as to their several claims, be and the same are hereby severally overruled, and the report of the Special Master with respect to each of such claims is hereby ratified and confirmed; and

FURTHER ORDERED that the exceptions filed to said report by Washington Properties, Inc., to the allowance of the claim of the District of Columbia for \$774.48 on account of water rent, be and the same is hereby overruled, and the report of the Special Master with respect to such claim is hereby ratified and confirmed; and

FURTHER ORDERED that said report be and the same is hereby referred back to the Special Master, and said Special Master be and he is hereby ordered to consider further the claim of the District of Columbia for penalties for delinquency in the payment of the personal property taxes reported by said Special Master to be due, and to report to the Court within ten days further additional find-

ings of fact and conclusions of law with respect to said claim, and that said Special Master may proceed upon this reference in his discretion without additional testimony, hearings or notice, except that notice of any hearing to be held before said Special Master and of the filing of his further report shall be given to counsel for the parties whose exceptions concerning said claim are hereinafter dealt with; and

50 FURTHER ORDERED that the exceptions filed by Washington Properties, Inc., and by Julius I. Peyser and Joseph P. Tumulty, receivers herein, to the allowance by the Special Master in his said report of the claim of the District of Columbia for personal property taxes in the sum of \$52,956.20, and the exceptions by the District of Columbia to the said report in so far as it fails to allow in addition to said amount for personal property taxes the penalties claimed by the District of Columbia to have accrued thereon, be and the same are hereby held under advisement by the Court, provided that additional exceptions may be filed to such further findings and conclusions as the Special Master may report with regard to said claim within ten days after the Special Master shall file his report, by Washington Properties, Inc., Julius I. Peyser and Joseph P. Tumulty, as receivers herein, and the District of Columbia, if said parties shall be so advised.

/s/ O. R. LUHRING
Justice.

From the foregoing an appeal noted in open Court by Counsel for The Walter M. Ballard Co. and Security Savings & Commercial Bank. Cost bond fixed at \$100.00 or cash deposit of \$50.00 in lieu thereof.

/s/ O. R. LUHRING,
Justice.

Feb'y. 18—1937

From the foregoing an appeal is noted in open Court for Edwin H. Brownley, Receiver for Wardman Realty & Construction Co. Cost bond fixed at \$100.00 or cash deposit of \$50.00 in lieu thereof.

/s/ O. R. LUHRING,
Justice.

Feb'y. 18—1937

Memorandum.

March 8, 1937.

\$50.00 cash deposited in lieu of bond for costs on appeal.

Assignments of Error.

Comes now Edwin H. Brownley, Statutory Receiver, Wardman Realty and Construction Company, by his attorney and for assignments of error on appeal to the United States Court of Appeals for the District of Columbia, shows:

1. The Court erred in overruling the exceptions of Edwin H. Brownley, as receiver for Wardman Realty and Construction Company, to the second and final report of the Special Master, A. Leftwich Sinclair, filed on the 9th day of April, 1936, denying the claim in the sum of \$186,656.52.

2. The court erred in not holding and deciding that the cash accounts receivable, inventories and choses in action belonging to the Wardman Realty and Construction Company on March 7, 1931, were assets of the said Company for the payment of its current debts for the maintenance and operation of its properties, and that the creditors of said Company, especially those who supplied services, goods, wares and merchandise in the normal course of business for the maintenance and operation of said properties, were entitled to the whole of said assets.

3. The court erred in not holding and deciding that the same directors who were directors of the Wardman Realty and Construction Company, the sole stockholder of the Wardman Real Estate Properties, Inc., and who were also directors of the Wardman Real Estate Properties, Inc., on March 7, 1931, acting for both corporations, unlawfully transferred and removed from the assets of the Construction Company practically the entire assets of the last named

Company, embracing goods, wares, merchandise,
52 cash and accounts receivable, aggregating \$266,-
016.09, besides other personal property not accounted for, and unlawfully transferred the same to the said Properties Company in fraud of the creditors of the said Construction Company.

4. That the court erred in upholding the action of the same directors acting for both Companies in preferring as creditors the Wardman Real Estate Properties, Inc., the

wholly owned subsidiary of the said Wardmsn Realty and Construction Company, the same being practically one Corporation.

5. The court erred in not holding and deciding that the claimant was entitled as Receiver of the Wardman Realty and Construction Company, to be paid out of the cash in the hands of the Receivers of the said Properties Company, the following items improperly charged by the said Receivers of the Wardman Real Estate Properties, Inc., against the said Wardman Realty and Construction Company, to wit:

Unpaid personal property taxes	\$30,684.80
Accrued real estate taxes	47,685.66
Inventories	27,318.24

(And in addition the value of the coal, hardware and other goods, wares and merchandise on hand at the time of the unlawful transfer and removal in bulk of the said assets to the said Properties Company)

6. The Court erred in not holding and deciding that the action of the identical directors of the two Companies, when the Wardman Realty and Construction Company was wholly insolvent in paying out of its funds to the detriment of those creditors who supplied services, goods, wares and

merchandise in the normal course of business for the
53 maintenance and operation of the said Properties Company, was not a fraud on such creditors of said Construction Company, and an accounting should be made thereof to the Receiver of the Construction Company for the protection of its creditors.

7. The court erred in holding and deciding that the agreement by which the Wardman Real Estate Properties, Inc., acquired all of the assets of the Wardman Realty and Construction Company was fair and to the best interests of the creditors of the Construction Company, since the same amounted to a preference of the Wardman Real Estate Properties, Inc., as a creditor of its wholly owned subsidiary.

8. The court erred in holding and deciding that the writing off of any supposed indebtedness for rent between the two corporations identically controlled, and in legal effect identical corporations, should not enure to the benefit of the

creditors of the Wardman Realty and Construction Company who dealt with said Corporation on the strength of its assets.

9. The court erred in other respects apparent on the face of the record.

/s/ LESLIE C. GARNETT
Attorney for appellant.

Service of copy hereof is hereby acknowledged this 8th day of March, 1937.

/s/ DOUGLAS, O'BEAR, MORGAN & CAMPBELL
Attorney for Julius I. Peyser and Joseph P. Tumulty, Receivers, Wardman Real Estate Properties, Inc.

/s/ PAUL E. LESH
Attorney for Washington Properties, Inc.

54 District Court of the United States for the
District of Columbia

Equity No. 53,117.

CENTRAL HANOVER BANK & TRUST Co., a body corporate, and
FRANK WOLFE, TRUSTEE, *Plaintiffs,*

v.

WARDMAN REAL ESTATE PROPERTIES, INC. a body corporate,
Defendant.

Equity No. 53,180.

RALPH P. COMPTON, *Plaintiff,*

v.

WARDMAN REAL ESTATE PROPERTIES, INC., a body corporate,
Defendant.

O-R-D-E-R

On motion of Leslie C. Garnett, attorney for Edwin H. Brownley, Statutory Receiver, Wardman Realty and Construction Company, it is this 10th day of March, 1937,

ORDERED, that the time for filing statement of evidence in this cause is extended for twenty days additional.

/s/ DANIEL W. O'DONOGHUE
Justice.

No objection.

/s/ DOUGLAS, O'BEAR, MORGAN & CAMPBELL,
by /s/ EDMUND D. CAMPBELL
*Attorney for Julius I. Peyser and Joseph P. Tumulty,
Receivers, Wardman Real Estate Properties, Inc.*

/s/ PAUL E. LESH
Attorney for Washington Properties, Inc.

55 District Court of the United States for the
District of Columbia

Equity No. 53,117.

CENTRAL HANOVER BANK & TRUST Co., a body corporate, and
FRANK WOLFE, TRUSTEE, *Plaintiffs,*

v.

WARDMAN REAL ESTATE PROPERTIES, INC., a body corporate,
Defendant.

Equity No. 53,180.

RALPH P. COMPTON, *Plaintiff,*

v.

WARDMAN REAL ESTATE PROPERTIES, INC., a body corporate,
Defendant.

O-R-D-E-R

On motion of Leslie C. Garnett, attorney for Edwin H. Brownley, Statutory Receiver, Wardman Realty and Construction Company, it is this 26th day of March, 1937,

ORDERED, that the time for filing statement of evidence in this cause is extended for twenty days additional, from March 30, 1937.

PEYTON GORDON
Justice.

No objection.

/s/ DOUGLAS, O'BEAR, MORGAN & CAMPBELL,
by /s/ HUGH H. O'BEAR

*Attorney for Julius I. Peyser and Joseph P. Tumulty,
Receivers, Wardman Real Estate Properties, Inc.*

/s/ PAUL E. LESH

Attorney for Washington Properties, Inc.

56 District Court of the United States for the
District of Columbia

Equity No. 53,117.

CENTRAL HANOVER BANK & TRUST Co., a body corporate, and
FRANK WOLFE, TRUSTEE, *Plaintiffs,*

v.

WARDMAN REAL ESTATE PROPERTIES, INC., a body corporate,
Defendant.

Equity No. 53,180.

RALPH P. COMPTON, *Plaintiff,*

v.

WARDMAN REAL ESTATE PROPERTIES, INC., a body corporate,
Defendant.

O-R-D-E-R

On motion of Leslie C. Garnett, attorney for Edwin H. Brownley, Statutory Receiver, Wardman Realty and Construction Company, it is this 15th day of April, 1937.

ORDERED, that the time for filing statement of evidence in this cause is extended for twenty days additional.

/s/ DANIEL W. O'DONOGHUE
Justice.

No objection.

/s/ EDMUND D. CAMPBELL

Attorney for Julius I. Peyser and Joseph P. Tumulty, Receivers, Wardman Real Estate Properties, Inc.

/s/ PAUL E. LESH

Attorney for Washington Properties, Inc.

57 *Stipulated Designation of Record for Appeal.*

The petitioner having perfected an appeal herein to the Court of Appeals of the District of Columbia on March 10, 1937, the undersigned counsel hereby request the Clerk of the District Court of the United States for the District of Columbia to prepare at petitioner's expense, a transcript of the record on appeal, including therein the following papers and proceedings, namely:

1. Final order of the Court dated February 18, 1937.
2. Receipt for \$50.00 cash deposited by petitioner in lieu of appeal bond.
3. Assignments of Error.
4. Order of March 10, 1937, of the District Court of the United States for the District of Columbia extending time for filing the statement of the evidence.
5. Order of March 26, 1937, of the District Court of the United States for the District of Columbia extending time for filing the statement of the evidence.
6. Order of April 15, 1937, of the District Court of the United States for the District of Columbia extending time for filing the statement of the evidence.
7. Agreed statement of the case.
8. Stipulated designation of record.

LESLIE C. GARNETT

Attorney for Appellant.

DOUGLAS OBEAR MORGAN and CAMPBELL

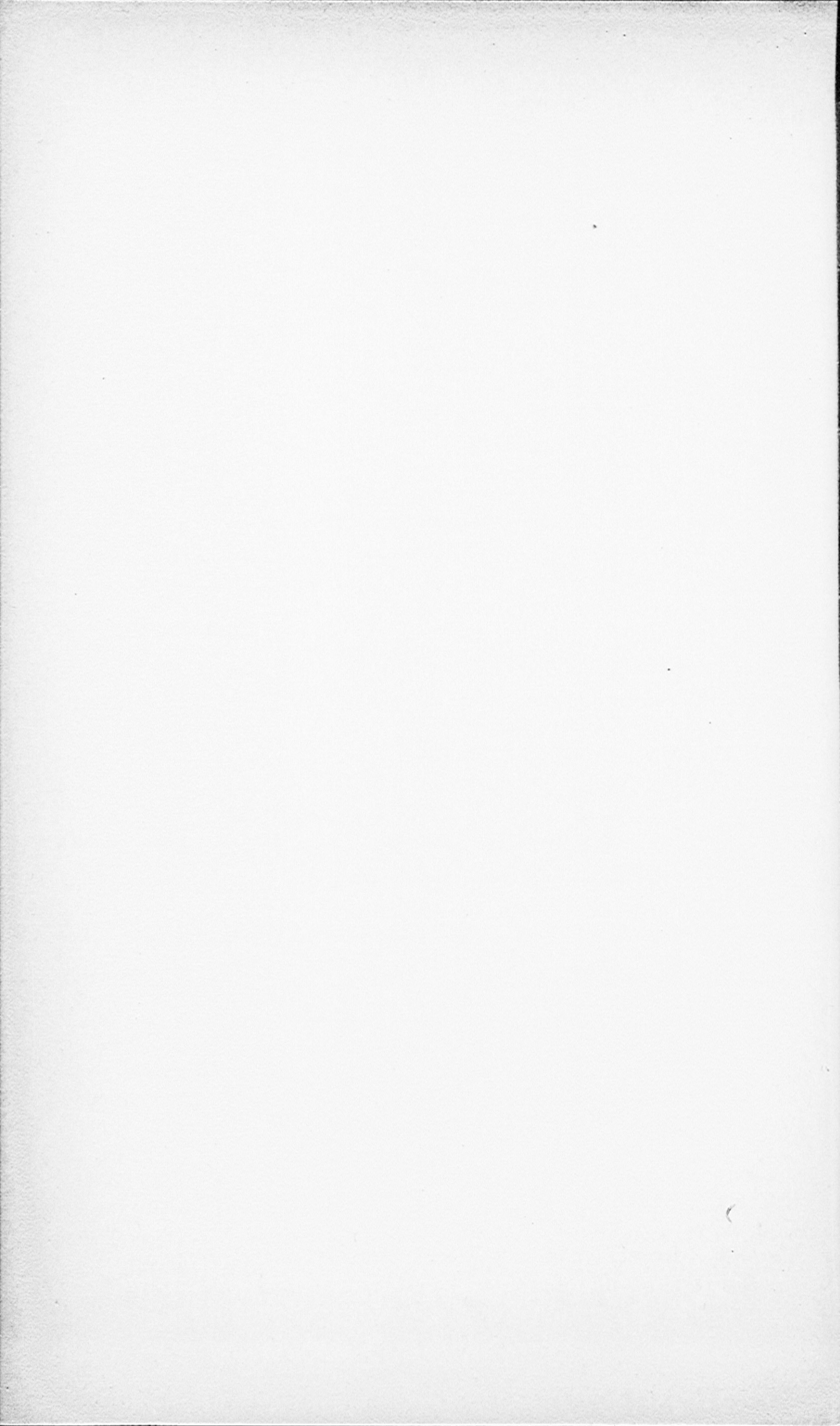
By EDMUND D. CAMPBELL

*Attorneys for Julius I. Peyser
and Joseph P. Tumulty, Re-
ceivers, Wardman Real Es-
tate Properties, Inc., Ap-
pellees.*

PAUL E. LESH,

*Attorney for Washington
Properties, Inc., Appellee.*

Endorsed on Cover: No. 6963. Edwin H. Brownley,
Statutory Receiver Wardman Realty and Construction
Company Appellant vs Julius I Peyser and Joseph P
Tumulty Receivers et al United States Court of Appeals
for the District of Columbia Filed May 4—1937 Moncure
Burke, Clerk



Addition to Record per Stipulation of Counsel

United States Court of Appeals for the District of Columbia

APRIL TERM, 1937.

No. 6963

**EDWIN H. BROWNLEY, STATUTORY RECEIVER,
WARDMAN REALTY AND CONSTRUCTION COM-
PANY, APPELLANT,**

vs.

**JULIUS I. PEYSER AND JOSEPH P. TUMULTY, RE-
CEIVERS, WARDMAN REAL ESTATE PROPER-
TIES, INC., AND WASHINGTON PROPERTIES,
INC.**

FILED JANUARY 27, 1938

MONCURE BURKE,
Clerk.

Stipulation.

It is stipulated by and between the appellant and the appellees that the following correction and addition be made to the record herein:

Strike out paragraph numbered XII (record printed page 25) of the "Agreed Statement of the Case", and substitute in lieu thereof the following:

XII. Central Hanover Bank and Trust Company, trustee under the deed of trust securing the first and refunding bonds of the Properties Company, on December 6, 1933, secured judgment against the Company, based on the aggregate amount due all such bondholders, \$13,374,036.56, less the net proceeds of foreclosure,

7(2)
\$2,903,997.47, leaving a deficiency for which said judgment was entered of \$10,470,039.09. Claim was made by said trustee in the latter amount against the unmortgaged assets held by the Receivers in Equity No. 53180 before the Special Master and was allowed in his report of April 9, 1936. The holders of approximately 93% in amount of the bonds entitled to share in the proceeds of this judgment and claim joined in the organization of Washington Properties, Inc., and transferred their bonds and claims thereon to it in exchange for new bonds and stock issued by it. Holders of \$2,080,500 of the senior debentures of the Construction Company had also transferred their debentures and the general (junior) mortgage bond for \$2,500,000 of the Properties Company (which they had acquired by foreclosure sale of said bond which had been security for their debentures) to Washington Properties, Inc., in exchange for stock issued by it. Holders of \$220,000 two years 6% notes of the Properties Company, dated September 1, 1928, had also transferred them to Washington Properties, Inc., in exchange for stock issued by it. The claim by Washington Properties, Inc., on said general mortgage bond and said two year notes, a total claim of \$2,270,000, was likewise allowed against said unmortgaged assets by said Special Master's report of April 9, 1936. The report was confirmed by the Court by its order of April 30, 1936, as to certain claims, including those aforesaid of Central Hanover Bank and Trust Company, trustee, and Washington Properties, Inc.

LESLIE C. GARNETT,
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Receiver, Appellant.*

EDMUND D. CAMPBELL,
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Joseph P. Tumulty, Receivers,
Appellees.*

PAUL E. LESH,
*Attorney for Washington
Properties, Inc., Appellee.*

UNITED STATES

~~COURT OF APPEALS FOR THE~~

DISTRICT OF COLUMBIA

FILED SEP 16 1937

IN THE

United States Court of Appeals

CLERK

FOR THE DISTRICT OF COLUMBIA.

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EDWIN H. BROWNLEY, STATUTORY RECEIVER, WARDMAN
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WASHINGTON PROPERTIES, INC.

—
Appeal from the District Court of the United States
for the District of Columbia.
—

BRIEF FOR APPELLANT.
—

LESLIE C. GARNETT,
Attorney for the Appellant.

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WASHINGTON PROPERTIES, INC.

Appeal from the District Court of the United States
for the District of Columbia.

BRIEF FOR APPELLANT.

This case comes up upon "Agreed Statement of the Case" (R. 2) and involves the claim of the appellant Brownley, Statutory Receiver of the Wardman Realty and Construction Company, hereinafter called the Construction Company, for certain of the unmortgaged

assets in the hands of the defendants Peyser and Tumulty as receivers of the Wardman Real Estate Properties, Inc., hereinafter called the Properties Company.

STATEMENT.

The Construction Company, organized under the laws of Maryland, owned all of the capital stock of the Properties Company, a corporation also organized under the laws of Maryland. These companies were simultaneously organized and up until February 26, 1931, had identical officers and directors (R. 15). The Properties Company held title, subject to mortgages, to Wardman Park Hotel, Wardman Park Addition, 2700 Connecticut Avenue, Cathedral Mansions Center, Cathedral Mansions North, The Highlands Apartment, Carlton Hotel, Department of Justice Building and Davenport Terrace Apartments. On July 15, 1929, the Properties Company leased these properties to the Construction Company (R. 2), and until February 26, 1931, the properties were operated by the Construction Company, with officers and directorate identical with those of the Properties Company. On February 26, 1931, the Construction Company being in default in rent in the sum of \$654,000 (R. 15) and being wholly insolvent, the officers and directors of the two companies were divided, and of these officers and directors some who had been officers and directors of both companies became officers and directors of one company only (R. 15). Immediately prior to the severance of officers and directors negotiations were being carried on for the cancellation of the lease between the two companies, and on March 17, 1931, an agreed cancellation of the lease was made effective as of February 28,

1931 (R. 16). Under this agreement of cancellation the officers and directors of the Properties Company and its sole stockholder the Construction Company transferred on the books of the two corporations from the Construction Company to the Properties Company assets of the Construction Company aggregating \$240,702.40 (R. 20). Charged against these assets were liabilities aggregating an identical amount (R. 21). Among these liabilities were:

Accrued personal property taxes	
(Schedule F, R. 22, 23), aggregating	\$30,684.60
Real Estate taxes (Schedule G, R. 21)	47,653.68
Inventories (Schedule B, R. 21)	27,547.09

In addition to the inventories referred to in Schedule B above, at the time of the cancellation of the lease there were coal, hardware, soaps, cleaning material and other goods, wares and merchandise on hand in the eleven apartment houses and hotels which were taken over by the Properties Company without adjustment between the two (R. 23).

The agreement of cancellation (R. 17) in addition to transferring to the Properties Company all operating cash, all merchandise and supplies on hand or in transit, also provided for the delivery of such deferred and prepaid items "as may be designated by the President of the Properties Company". This agreement further provided (R. 18-19) that the Properties Company should pay such operating accounts as "shall be selected within twenty days from the date hereof by the President of the Properties Company". The agreement further provided that the Properties Company should pay accrued liabilities of the Construction Company, "such accrued liabilities to be designated by the President of the Properties Company".

It appears that the deferred and prepaid items of \$68,022.70 (Schedule C, R. 20), the amounts assumed by the Properties Company (Schedule F, R. 21) as accrued liabilities, \$73,498.87, and the accounts payable (Schedule E, R. 21), \$119,549.85, were all selected or designated by the President of the Properties Company, leaving to the Construction Company only such assets, which were negligible, as the President of the Properties Company did not select.

The Construction Company, as of September 1, 1928, had issued \$2,500,000 Senior Debenture bonds and \$2,400,000 Junior Debenture bonds, all of which were outstanding at the time of the cancellation of the lease and the taking of all the assets of the Construction Company by the Properties Company.

The Properties Company had outstanding \$10,963,000 First and Refunding Mortgage bonds at the time of the cancellation of the lease, and had issued a \$2,500,00 General Mortgage Junior to the First and Refunding bonds (R. 24).

The sale of the properties at the suit of the trustee was decreed by the District Court of the United States for the District of Columbia October 14, 1931, and sale was made October 21, 1932. The appellee, Washington Properties, Inc., became the final purchaser and title was conveyed to that corporation (R. 24). A deficiency judgment was awarded to the appellee, Washington Properties, Inc., in the sum of \$10,470,039.09 (R. 25).

On the 31st day of July, 1931, in Equity cause No. 53,180, being a general creditors' suit, the same receivers were appointed receivers of all the unmortgaged assets of the Properties Company in the District of Columbia, and they now have on hand in this

receivership the sum of approximately \$197,917.30 (R. 24). On April 19, 1933, the District Court referred both equity causes to a Special Master and directed all persons having claims or demands against the Properties Company or the receivers, or against any property in the hands of the receivers, to file the same (R. 25); and the appellant Brownley, as receiver of the Construction Company, seasonably filed a claim that out of the unmortgaged assets of the Properties Company, into which fund all of the assets of the Construction Company were carried, the receiver of the Construction Company should receive at least the difference between the assets of the Construction Company which the Properties Company took, and the accounts carried as payable upon the books, or the aggregate of the accrued personal property taxes, \$30,684.60, the real estate taxes, \$47,653.68, the inventories, \$27,547.09, and the amount shown by the books to have been paid by the Construction Company after its insolvency was known on the permanent improvements of the buildings of the Properties Company, aggregating \$25,000. (R. 28-35).

After hearing the Special Master on April 9, 1936, submitted his final report rejecting in toto the claim of the appellant (R. 35-38). The appellant Brownley, Statutory Receiver, filed exceptions to this report (R. 39), which exceptions were overruled by the Court in a memorandum (R. 41), and by order of February 18, 1937 (R. 42).

THE APPELLANT'S CONTENTIONS.

It is contended on behalf of the appellant that:

1. A Court of equity will look behind the corporate fiction in order to do justice, and will not permit the

Properties Company to be a creditor, preferred or otherwise, of its sole stockholder the Construction Company under a lease executed by identical officers and directors for both corporations.

2. In asserting a claim for the assets of the Construction Company unlawfully transferred to the Properties Company, the creditors of the Construction Company are not asserting a preference against the assets of the Properties Company, but are merely insisting that equity will decree that the creditors of the Construction Company shall be paid out of the assets of the Construction Company, leaving the creditors of the Properties Company to be paid out of the assets of the Properties Company.

ARGUMENT.

I.

A Court of equity will look behind the corporate fiction in order to do justice, and will not permit the Properties Company to be a creditor, preferred or otherwise, of its sole stockholder the Construction Company under a lease executed by identical officers and directors for both corporations.

It appears from the statement above and from the record that with identical officers and directors of these simultaneously organized corporations, \$11,000,000 of securities were floated by the Properties Company based upon the value of these properties. These securities were denominated "First and Refunding Bonds", although issued subject to a \$5,000,000 mortgage on some of the properties.

Likewise, the Construction Company issued \$4,900,000 of securities based upon the lease from its wholly

owned subsidiary the Properties Company. The court in considering the issuance of these securities said in *Thomas, et al. v. Central Hanover Bank & Trust Company*, 75 Fed. (2nd) 227, 231:

“Our conclusion based upon the very unsatisfactory record before us, is that the charges of fraud made against the New York bankers relative to the inception and organization of the Wardman Real Estate Properties, Inc., as a corporation and the issuance and sale of \$11,000,000 of mortgage bonds secured by mortgage upon the real estate held by the corporation seem to be probably correct.”

From the record it fairly appears that the separate corporate existence of these corporations served the purpose of the promoters and those who were responsible for floating these securities to swell the amount of the corporate indebtedness. One corporation was wholly the creature of the other, and a separate corporate entity was used to acquire credit, absorb any operating loss without charge on the properties, and pyramid the sale of securities. When the assets of the Construction Company were bodily lifted into the coffers of the Properties Company the assets and liabilities being designated by the President of the Properties Company,—this was merely trading pockets in the same trousers and by this device seeking to conceal the assets of the Construction Company from its creditors and to prefer the Properties Company itself as a creditor.

The court below gave no reason for its action, but the Special Master in denying the claim of the appellant and discussing this lifting of the assets from one corporation to the other, says (R. 37):

“and that in the absence of a showing of bankruptcy occurring within four months, the transfer could at most have been regarded as a preferential payment by the Realty and Construction Company to one of its principal creditors.”

It must be remembered that the only alleged indebtedness of the Construction Company to the Properties Company, other than the promise of the Construction Company to pay the taxes on the Properties Company's properties, was the \$654,000 rental under the lease. This lease was entered into by identical officers and directors of both corporations and was in effect a contract made by one corporation with itself. This conclusion is inescapable and is buttressed by the fact that after the Properties Company had absorbed all the assets of the Construction Company it wrote off this claim down to \$1.00. From the history of the litigation it evidently was an oversight that the Properties Company did not get a deficiency judgment against itself for the difference between \$654,000 and the \$240,702.40 of assets of the Construction which it covered into its own treasury.

This is a clear fraud on the creditors of the Construction Company and this wrong cannot be justified by the claim of the separate corporate entity of the parent company and its wholly owned subsidiary.

The fiction of distinct corporate entity is disregarded when necessary to do so in order to circumvent fraud and also when a corporation is so organized and controlled and its affairs are so conducted as merely to make it an instrumentality or adjunct of another corporation. *Hunter v. Baker Motor Vehicle Co.*, 225 Fed. 1006, 1015, 1016. In the latter case the court was considering a controversy involving the Baker Motor

Vehicle Company of Ohio and the Baker Motor Vehicle Company of New York, and in denying the claim of the parent company to the assets of the other corporation, its instrumentality, said:

“The Ohio company was and is, of course, entitled to all of the property and all of its proceeds after paying all the creditors. The Ohio Company was not and is not a creditor entitled to share in that property or its proceeds as against its other creditors. In *Re Watertown Paper Company*, 169 Fed. 252, 255.”

Many other cases on the subject are reviewed in *U. S. v. United Shoe Machinery Company*, 234 Fed. 127, 141, 142. The court said:

“Whatever may have been the views of the courts in the early days of corporate existence, when there were but few corporations, and they mostly confined to business of a quasi public nature, at this date courts, and especially courts of equity, will look behind the corporate fiction, and if it clearly appears that one corporation is merely a creature of another, the latter holding all the stock of the former, thereby controlling it as effectively as it does itself, it will be treated as the practical owner of the corporation, when necessary for the purpose of doing justice.”

In *Chicago, Milwaukee & St. Paul Railway Company v. Minneapolis, etc.*, 247 U. S. 490, the Supreme Court citing a number of cases said that where the subsidiary company was used as an instrumentality or agency of the owning company the courts would not permit themselves to be blinded or deceived by mere forms of law, but would deal with the substance of the transaction “as if the corporate agency did not exist and as the

justice of the case may require." See also *United States v. Union Stockyards*, 226 U. S. 286; *United States v. Lehigh Valley R. R. Co.*, 254 U. S. 255; *United States v. Reading Co.*, 253 U. S. 26.

In *McIlhenny v. Lampton*, 45 W. L. R. 22, Chief Justice McCoy held that it was a fraud for Lampton to organize a corporation to whom his earnings as a real estate operator were being paid and thus escape his judgment creditors. The appropriate syllabus in this case is as follows:

"Where an individual owns practically all of the stock of a corporation and controls all of its operations, he and the corporation are in proper cases regarded as one and the same."

This court in *Eichelberger v. Arlington Building*, 52 App. D. C., 23, 25, recognized the exceptions to the entity rule in the following language:

"But there is an exception to the entity rule, where its recognition would result in promoting illegality, fraud, or injustice. In other words, since the franchise is granted by the state for a useful and valid purpose, it may not be employed to further wrong. Where it is so employed the law will disregard the rule, go behind the fiction, and treat the stockholders as if the corporation did not exist. *McCaskill Co. v. United States*, supra; *United States v. United Shoe Machinery Co. (D. C.)* 234 Fed. 127; *Linn & Lane Timber Co. v. United States*, 236 U. S. 574, 35 Sup. Ct. 440, 59 L. Ed. 725; *State v. Standard Oil Co.*, 49 Ohio St. 137, 30 N. E. 279, 15 L. R. A. 145, 34 Am. St. Rep. 541."

Since both the Construction Company and the Properties Company are Maryland corporations, it might

be well to turn to the expressions of the Maryland courts as to the right of one corporation owning all of the stock of the other corporation to make that company subservient to its own interests.

Among cases in which this subject is discussed is *Davis v. U. S. Electric, etc. Co.*, 77 Md. 35, where it is said, p. 40:

“The gravamen of the complaint made by the bill is, that the Brush Co., having obtained control of the management of the United States Co., is using its power to make that company subservient to its own interest, to use it as a feeder, and finally utterly to destroy it, whenever it shall be to their profit so to do. This, as was said in *Booth v. Robinson*, supra, would be a fraud of the most flagrant character. It would subject the corporation at whose instance the scheme was devised and executed, not only to a civil liability for the injury done, but also to the penalties of misuser or abuser of its franchises; and in such a case ‘Courts can neither be too emphatic in condemning the act, nor too ready to afford the strongest remedy allowed by law for the prevention or redress of the wrong.’”

In *The James Clark Co. v. Colton*, 91 Md. 195, the Court considered whether or not payments made by a bank to its officers and agents at a time when it was insolvent, to the exclusion of and in detriment of other creditors of the bank were unlawful preferences within the meaning of the insolvent law of Maryland. The Court held that officers of a corporation, who are also its creditors, cannot lawfully pay their own claims in preference to other creditors, when the corporation is insolvent, and that when it became evident that the corporation was so embarrassed that it could not con-

tinue to conduct business and was unable to pay all of its debts in full, the directors are to be treated as trustees for all the creditors, although the corporation may not have been adjudged insolvent. It further held that the invalidity of such preferences did not depend upon the provisions of the Insolvent Law, but resulted from the unfair character of the transaction and its violation of the equitable principle that all creditors should be treated with equality.

In *Folsom & Co. v. Detrick Fertilizer Co.*, 85 Md. 52, the Maryland Court considered the transfer of properties between a debtor and a corporation wholly formed by the debtor. This was held to be in fraud of creditors, the Court saying (p. 69):

“These transactions were technically and legally corporate acts; but in reality and substance they were the acts of Wooldridge and Folsom & Co. bearing corporate form and having the corporate authority. They had entire control of the corporation, and managed it according to their own wishes. They necessarily knew that in the course of its business of buying, selling and manufacturing, it would contract debts; and that when it obtained credit, it would be on the faith of its apparent resources, and with the belief and expectation on the part of creditors that its earnings would be applied to the payment of debts contracted in the course of its business. But by the purchase which they made for it in the corporate name and the debts which they caused it to assume they sought to devote these resources and earnings to the payment of debts due by one of themselves to the other, and to third persons. Now, any one may readily see that if this purpose had been made known to persons dealing with the corporation, it would never have obtained credit. The purpose contemplated great injustice to fu-

ture creditors. It was nothing less than a defeat of their claims. It took from them a fund which, according to the regular course of business, they had a right to believe would be applied to the debts due them. And it took it to pay debts unjustly imposed on the corporation by persons who controlled its action and sacrificed the corporate interest for their own private benefit.”

See also *Bauernschmidt v. Bauernschmidt*, 101 Md. 148; *In Re Bauernschmidt's Estate*, 97 Md. 35.

It would seem that those who were negotiating the transfer of all the assets of the parent company to its wholly owned subsidiary sensed the eleventh hour necessity of some divergence between the interests of the corporations in order that one might transfer to the other all of its assets, for we find from the record (R. 15) that immediately prior to the severance of officers and directors negotiations were being carried on between these identical officers and directors, some of whom shortly afterwards remained exclusively officers of the Properties Company and some exclusively officers of the Construction Company, for a cancellation of the lease. The purpose, therefore, of the severance was that the Properties Company might get for itself such assets of the parent company as the President of the subsidiary might select, and the cancellation was made effective as of two days after the severance of officers and directors between the companies.

It is therefore confidently asserted that the court below erred in sustaining the holding of the Special Master that the transfer of the assets from the Construction Company to the Properties Company was merely a preferential payment by the Construction Company to one of its principal creditors, and that

such payment was lawful. It seems too plain for argument that these officers and directors could not sit around a table and transfer the funds of the Construction Company to the Properties Company to swell the assets of the Properties Company, and thus deprive the Construction Company of the funds necessary to pay its obligations to those who dealt with it and relied upon its assets in so dealing.

The summary of schedules (R. 20) shows that after deducting \$25,312.69 as a reserve from the accounts receivable the Properties Company took over assets of the Construction Company aggregating \$240,702.40. To off-set these assets there was charged against the Construction Company as a part of the liabilities heretofore set out \$47,653.68 of real estate taxes chargeable against the Properties Company's real estate. This was a clear preference by the subsidiary of itself as a creditor of the parent company. Another liability charged against the Construction Company in this transfer of assets was the sum of \$30,684.60 (R. 23) of personal taxes which have never been paid and which are barred, and which are clearly a credit of the Construction Company which should go to its creditors. The Properties Company took for its own purposes and for its own use \$27,547.09 of inventories, wholly the property of the Construction Company. This is a violation of at least the spirit of the Bulk Sales Act of the District of Columbia and is another attempt to conceal from the creditors of the Construction Company these assets. In addition to the inventories taken over by the Properties Company there were coal, hardware, soaps, cleaning material and other goods, wares and merchandise on hand in the eleven apartment houses and hotels taken by the Prop-

erties Company without adjustment between the two companies (R. 23). We assert that the Properties Company was not and is not a creditor entitled to share in the property of the Construction Company or its proceeds, as against its other creditors, *Hunter v. Baker Motor Vehicle Company, supra*. Therefore it was unlawful and in fraud of creditors for the officers and directors of the parent company and of its wholly owned subsidiary to take over all the assets of the parent company, thus not only assuming the position of a creditor, but a preferred creditor.

II.

In asserting a claim for the assets of the Construction Company unlawfully transferred to the Properties Company, the creditors of the Construction Company are not asserting a preference against the assets of the Properties Company, but are merely insisting that equity will decree that the creditors of the Construction Company shall be paid out of the assets of the Construction Company, leaving the creditors of the Properties Company to be paid out of the assets of the Properties Company.

It was asserted in argument in the court below that to allow the claim of the appellant would be to prefer the Construction Company as a creditor in the receivership proceeding.

We reiterate that the action of the two corporations in lifting the assets of the parent company into the treasury of the subsidiary was a fraud upon the creditors of the parent company who dealt with it upon the strength of its assets. These assets are reflected

in the unmortgaged assets now in the hands of the receivers, aggregating \$197,917.30 (R. 24). It is undenied that the real estate taxes were charged against the Construction Company; that the personal property taxes were likewise charged but were not paid and are barred, and that the inventories were taken over by the subsidiary. These four items aggregate \$105,885.37. This leaves out of consideration the sworn claim of the appellant that after the insolvency of the Construction Company was known, the books of the two companies which were before the Auditor reflected that in the operation of the properties under identical officers and directors there was paid out of the treasury of the Construction Company on permanent improvements to the buildings of the Properties Company more than \$25,000.

The appellant is entitled to an accounting for all the assets unlawfully acquired by the Properties Company and now reflected in the unmortgaged assets in the hands of the receivers, the least sum to which appellant is entitled being the \$105,885.37, above set out. This is merely rendering unto Caesar the things that are Caesar's—giving to the creditors of the Construction Company the assets of that company and leaving to the Properties Company its assets for the benefit of its creditors.

CONCLUSION.

The appellee, Washington Properties, Inc., now holds title to all the real estate of the Properties Company acquired under the receivership. Its president and some of the other officers are the same individuals who were officers of the Properties Company. The court below in affirming the sale of these properties to

the appellee expressed regret that the price received did not bear a better relation to the assessed value and market value of the real estate. *Thomas v. Central Hanover Bank & Trust Company, supra*, p. 231. Mr. Justice Groner in his dissenting opinion in the *Thomas case, supra*, p. 233, joined in by the late Justice Hitz, pointed out that the purchase price was only about 28 per cent of the appraisal of the properties for taxation, and was less than the amount receivers had been offered for Wardman Park alone, and further that the price was "grossly inadequate".

The appellee, Washington Properties, Inc., was also awarded a deficiency judgment in the sum of \$10,470,-039.09 (R. 25).

The practical result, therefore, of the decree below is to give to this appellee, the holder of the deficiency judgment who acquired all of the real estate of the Properties Company at a grossly inadequate price, practically the entire unmortgaged assets, leaving the creditors of the Construction Company wholly out in the cold. This inequitable result should not be countenanced by a court of conscience. The order of the court below confirming the report of the Special Master overruling the exceptions of the appellant to the said report denying his claim in full should be reversed and the cause should be remanded to the District Court for a full accounting to the appellant of all the assets of the Construction Company unlawfully acquired by the Properties Company.

Respectfully submitted,

LESLIE C. GARNETT,
Attorney for the Appellant.

IN THE
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District of Columbia

No. 6963.

EDWIN H. BROWNLEY, Statutory Receiver, Ward-
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APPELLANT,

v.

JULIUS I. PEYSER AND JOSEPH P. TUMULTY,
Receivers, Wardman Real Estate Properties, Inc.,
and Washington Properties, Inc.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES
FOR THE DISTRICT OF COLUMBIA.

BRIEF ON BEHALF OF APPELLEES JULIUS I.
PEYSER AND JOSEPH P. TUMULTY, RECEIV-
ERS OF WARDMAN REAL ESTATE PROPER-
TIES, INC.

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DOUGLAS, OBEAR, MORGAN & CAMPBELL,
Of Counsel.

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Receivers, Wardman Real Estate Properties, Inc.,
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**BRIEF ON BEHALF OF APPELLEES JULIUS I.
PEYSER AND JOSEPH P. TUMULTY, RECEIV-
ERS OF WARDMAN REAL ESTATE PROPER-
TIES, INC.**

Statement.

The controversy represented by this appeal is a controversy between the receiver of a parent corporation and the receiver of its wholly owned subsidiary. In its final essence it is a controversy between the appellant, representing the sole stockholder of Ward-

man Real Estate Properties, Inc. and the appellees as the representatives of its creditors. The appellant is statutory receiver of Wardman Realty & Construction Company (hereafter for convenience sometimes called the "Construction Company") which is the parent corporation, and which is the sole stockholder of Wardman Real Estate Properties, Inc. (hereafter for convenience sometimes called the "Properties Company"). The appellees are receivers of the assets of the Properties Company.

The appellant, representing a corporation which was sole *stockholder* of the Properties Company, seeks to recover from the receivers of the Properties Company assets which the stockholder had turned over to it, (for a valuable consideration) four and a half months prior to receivership proceedings involving both corporations. Unfortunately the facts are somewhat complicated, and because of the inadequacy of the statement in appellant's brief, they must be here restated in full.

This case arises as an aftermath to the large scale financing of certain properties formerly owned by the Wardman interests in the District of Columbia. The foreclosure of these properties under a first and re-funding mortgage has heretofore been considered by this Court in the case of *Thomas et al. v. Central Hanover Bank & Trust Company*, 64 App. D. C. 96. The receiver of the Construction Company by these proceedings is seeking to recover from the receivers of the Properties Company certain so-called "un-mortgaged" assets remaining in the hands of the

Properties Company receivers, following the foreclosure sale referred to.

Wardman Real Estate Properties, Inc. was formed in October, 1928, to take title to and possession of certain valuable Wardman properties in the District of Columbia, including Wardman Park Hotel, the Carlton Hotel, the old Department of Justice Building and a number of apartment buildings (R. 2). On these properties it placed a first refunding mortgage bond issue of \$11,350,000 (R. 24).

The entire stock of Wardman Real Estate Properties, Inc. was issued to and has always been owned by Wardman Realty & Construction Company (R. 2), which stock therefore, in effect, represented the purported equity in the real properties referred to above, subject to the first and refunding mortgage of the Properties Company. Based upon this alleged equity, the Construction Company (*i. e.* the parent corporation) issued its own certain senior and junior debenture bonds aggregating \$4,900,000 (R. 24). These debentures, which were in reality backed by the purported equity in the properties of the subsidiary corporation (represented by a pledge of its stock) (R. 30, 31), were also partially secured by a \$2,500,000 "general mortgage bond" which the Construction Company had caused the Properties Company to issue and pledge with it as additional collateral (R. 24). The Construction Company and the Properties Company had the same officers and directors (R. 15).

Almost a year after the above financing (*i. e.* on July 15, 1929), the Properties Company entered into a

lease with its parent corporation (Construction Company) by which the Properties Company leased the properties covered by its first and refunding mortgage bond issue to its sole stockholder (the Construction Company). (R. 2.) Said lease, which was to run for a ten year term, was specifically made subject to the first and refunding mortgage of the Properties Company. No fixed rent was reserved to the lessor under said lease, but the Construction Company obligated itself to pay as rent all interest and amortization requirements and taxes under the first and refunding mortgage of the Properties Company (R. 5, 8), and all sums necessary for repairs and upkeep of the properties (R. 6, 7). It is significant to note that the debentures of the Construction Company were *not* based upon this lease, as stated by appellant's counsel in his brief (p. 6), but these debentures were in fact issued more than nine months before the lease was made (R. 2, 24).

Upon the execution of this lease in July, 1929, the Construction Company took over from its subsidiary the Properties Company, the management of the properties belonging to the latter. During the next year and a half, or until February 26, 1931, the Construction Company collected the rental income from said properties and paid all interest on its own debentures (R. 24), which debentures were, of course, *junior* in lien to the first and refunding mortgage bonds of the Properties Company; but while it applied this rental income to the payment of interest on its own junior securities the Construction Company defaulted in the

payment of rent to the Properties Company represented by the interest and amortization requirements on the first and refunding mortgage upon the properties and taxes thereon in the amount of \$654,000 (R. 15), and had accrued liabilities and accounts payable arising solely out of its operation of these properties amounting to \$193,048.72 (see schedules E and F, R. 21).

Under this state of facts which existed in February, 1931, it was agreed that the lease between the two companies should be cancelled and the operations of the properties returned to the Properties Company (R. 15, 16).

It was in connection with the cancellation of the lease between the two companies that there occurred the acts of which the appellant complains, and which acts are provided for in the cancellation agreement made between the two companies (R. 16-23).

The substance of this cancellation agreement was as follows:

(a) The Construction Company agreed to assign and turn over to the Properties Company cash in hand, inventories, prepaid items and accounts receivable in its possession *derived solely from its operation of the properties owned by the Properties Company*, amounting to \$240,702.40 (R. 17, 20).

(b) The Properties Company on its behalf agreed to assume and pay accrued and unpaid liabilities of the Construction Company arising solely out of the Construction Company's operation of the properties, and

real estate taxes which the Construction Company was obligated by the lease to pay, in an equal aggregate amount to the assets so taken over, *i. e.* \$240,702.40 (R. 19, 21).

(c) The prior indebtedness of the Construction Company to the Properties Company in the amount of \$654,000 was in no way affected by this agreement (R. 25).

Pursuant to the above mentioned agreement, the Construction Company did assign and turn over to the Properties Company the assets referred to, and the Properties Company on its part did pay for the Construction Company all of the obligations which it had agreed under the cancellation agreement to pay, except claims aggregating \$924 which were in dispute and except personal property taxes which have since been asserted by the District of Columbia as direct *preferred* claims against the Properties Company and which are now in litigation and on appeal to this Court (R. 23).

It may be noted in passing that the obligations of the Construction Company, assumed and paid by the Properties Company under this cancellation agreement, represented actually all of the ordinary trade accounts of the Construction Company (R. 36); that no part of the \$240,702.40 in assets turned over by the Construction Company to the Properties Company was applied by the latter on account of the past due indebtedness of the Construction Company to the Properties Company, but that said assets were used for the payment of the Construction Company's own

creditors other than the Properties Company; and that after the cancellation of the lease between the two companies the Construction Company still retained other assets not assigned to the Properties Company (R. 23).

In connection with the cancellation of the lease and the surrender of the properties by the Construction Company to the Properties Company, the Properties Company took over, without adjustment, certain coal, hardware, soaps, cleaning material and other merchandise on hand in the apartment houses and hotels. The same procedure had been followed between the two companies at the time the lease was entered into, at which time the Construction Company took over similar assets without adjustment (R. 23, 24).

About four and a half months later, *i. e.* in July, 1931, both companies went into receivership, the Wardman Realty & Construction Company by statutory proceedings in Maryland, and the Wardman Real Estate Properties, Inc. by proceedings involving its assets in the District of Columbia (R. 24, 28). The Maryland court appointed the appellant as receiver of the Construction Company; the District of Columbia court appointed the appellees receivers of the Properties Company, for both its mortgaged property and for its assets in the District of Columbia not covered by mortgage (R. 24). Thereafter the mortgaged property of the Properties Company was sold at foreclosure under its first and refunding mortgage to the appellee Washington Properties, Inc. (R. 24), (which sale was later confirmed by this Court in *Thomas v. Central*

Hanover Bank & Trust Company, supra), for a price much less than the first and refunding mortgage. Following this foreclosure there remained *unmortgaged* assets of Wardman Real Estate Properties, Inc. (consisting of cash, accounts receivable, etc.) in the hands of the appellee receivers amounting to \$197,917.30 (R. 24).

In April, 1933, the lower court referred the cause to the Auditor as special master for the purpose, among others, of receiving and passing upon claims which might be filed by any person, firm or corporation against Wardman Real Estate Properties, Inc. or the receivers, or against any property in their hands (R. 26). Many claims were filed with the special master and a large number of them allowed by him and by the court, including a deficiency judgment on the first and refunding mortgage bonds amounting to \$10,470,039.09, which deficiency judgment, of course, inures to the benefit of *all* holders of these first and refunding mortgage bonds.

The appellant Brownley, as receiver of the Wardman Realty & Construction Company, filed a claim with the special master (R. 28) seeking to recover from the appellees certain of the moneys which the Construction Company had paid to the Properties Company under the above mentioned cancellation agreement. Testimony was heard on the claim, and the special master made certain findings of fact, and disallowed the claim in its entirety (R. 35-38). The lower court upheld the special master in disallowing the claim, and from its order of disallowance this appeal is taken.

The appellant Brownley on this appeal has abandoned certain of the claims which he made before the special master. He seeks now to recover from the receivers of Wardman Real Estate Properties, Inc. moneys representing only certain of the assets which the Properties Company took over under the cancellation agreement, as follows:

Moneys equivalent to personal property taxes of Construction Company, assumed by Properties Company	\$30,684.80
Real estate taxes due by the Construction Company and assumed by the Properties Company	47,685.60
Inventories	27,318.24
Value of coal, hardware, etc. taken over by Properties Company from Construction Company without adjustment, estimated to be of a value between \$5,000 and \$25,000 (See special master's report, R. 36).	

In the brief of the appellant reference is made (p. 5) to an amount alleged to have been paid by the Construction Company for permanent improvements on the buildings of the Properties Company aggregating \$25,000 during the four months period prior to the cancellation agreement between the two companies (R. 33). No exception was taken to the disallowance of this portion of appellant's claim by the court below, and the statement with respect to it therefore has no proper place in appellant's brief.

Position of appellee receivers with respect to the issues involved.

The appellees Julius I. Peyser and Joseph P. Tumulty, as receivers of Wardman Real Estate

Properties, Inc., have no interest in the determination of the issues presented by this appeal, except to perform their duty as officers of the court. When the cause came before the Special Master the receivers were asked by him to take a position in the nature of *amicus curiae* with respect to each claim filed, and to recommend the allowance or disallowance of each claim as the case may be. The receivers have deemed it their duty to attempt to protect the fund in their custody against manifestly improper claims, but they do not wish to be considered as assuming a partisan position in disputes between respective claimants. They ask that the court consider the argument here contained in the light of these statements.

ARGUMENT.

I.

Consideration of question presented by appeal on basis of recognition of the separate corporate entities of Wardman Real Estate Properties, Inc. and Wardman Realty & Construction Company.

Despite the identity of officers and directors of the two companies and despite the fact that the Construction Company owned all of the stock of the Properties Company, it is not believed that this court should disregard the separate corporate entities of the two companies for the purposes of this case; for although the two corporations were under the same control they had and still have different classes of creditors who look to different groups of assets for the satisfaction of their respective claims. Assuming the

corporations to be considered as separate entities, the appellant finds himself in the position of representing the stockholders of Wardman Real Estate Properties, Inc. in a suit to recover assets of that corporation before the corporation's creditors are paid.

The appellant contends that the assets in question were not in reality assets of the Properties Company at all, but that they remained assets of the Construction Company as its sole stockholder, on the ground that the cancellation agreement between the two companies was constructively fraudulent and imposed a trust in the Properties Company to return these assets.

It is believed that the record fails to substantiate any charge of unfairness on the part of the Properties Company against the Construction Company in the transfer of these assets. The assets so turned over by the Construction Company to the Properties Company were all derived by the Construction Company from the very operation of the properties belonging to the Properties Company (R. 17, 18). The Construction Company, although obligated to pay taxes on the properties and interest and amortization requirements for the benefit of the First and Refunding Mortgage bondholders of the Properties Company, had in fact defaulted in the payment of this rental, and had suffered the First and Refunding Mortgage to become in default while it applied the income from the properties for the benefit of its own junior creditors (R. 24). The cancellation agreement when made was believed to be for the best interests of all concerned (R. 37). The Properties Company in consideration of the payment

to it of the sum of \$240,000 under the said cancellation agreement assumed and agreed to pay liabilities of the Construction Company arising out of the operations of the properties by the Construction Company, in an equal amount, which liabilities represented all of the ordinary trade accounts of the Construction Company (R. 36); and the Properties Company in compliance with this agreement did in fact pay all of the liabilities of the Construction Company which it had so assumed, with the exception of a \$924.00 claim in dispute and with the exception of personal property taxes, as to which a direct preferred claim has been asserted against the receivers of the Properties Company by the District of Columbia, and which claim is now in litigation and will shortly be before this Court for hearing (R. 23). In addition to these facts it will be noted that the indebtedness of the Construction Company to the Properties Company in the amount of \$654,000 was not affected by this agreement (R. 25) that the Construction Company retained other assets which it did not assign to the Properties Company under the cancellation agreement (R. 24); and that no bankruptcy proceedings were thereafter instituted against either the Properties Company or the Construction Company.

Under all of these circumstances it is not believed that the cancellation agreement could be considered as unfair to the Construction Company. No tender is now made by the receiver of the Construction Company to repay to the receivers of the Properties Company the moneys which the latter have already paid on account of the Construction Company's liabilities

assumed by the Properties Company under the agreement; and of course no such tender can be made, for it would more than offset the entire amount which the receiver of the Construction Company here seeks to recover.

It is believed, therefore, that the Special Master was right in holding that "the Realty and Construction Company apparently received full present consideration for the assets transferred by it to Wardman Real Estate Properties, Inc., under the agreement of March 7, 1931; * * * that in the absence of bankruptcy occurring within four months, the transfer could at most have been regarded as a preferential payment by the Realty and Construction Company to one of its principal creditors;" and in further holding that "to permit Wardman Realty and Construction Company to recover the sums claimed, under the circumstances disclosed, would be inequitable and unfair to the creditors of Wardman Real Estate Properties, Inc., and contrary to law." (R. 37.)

In this connection attention may be called to the well established rule of this court that findings of an auditor (or master) concurred in by the court below, are entitled to great weight and will not be set aside by this court except in exceptional circumstances.

France v. Coleman, 29 App. D. C. 286.

Richardson v. Van Auken, 5 App. D. C. 209.

Hutchins v. Munn, 28 App. D. C. 271.

II.

Consideration of question presented by appeal on basis of ignoring the separate corporate entities of the Construction Company and the Properties Company.

It is not believed that the appellant's position is improved by ignoring the separate corporate entities of the two corporations here involved, as he seems to wish to do.

If the separate corporate entities are ignored we must then assume that one corporation owned the real properties in question subject to a first and refunding mortgage of \$11,350,000 (R. 24) which it had suffered to become in default, by failure to pay taxes; that it had applied rental income from the property to its unsecured debentures while not applying it to the ordinary operating expenses of the property and to the mortgage debt itself. With such a state of facts existing on March 7, 1931, the company then caused \$240,000 of this accrued rental income from the properties to be applied to the payment of operating expenses of the properties and to taxes and other debts which it was obligated to pay by the terms of the mortgage, retaining, however, its equity in the properties and certain other assets. Foreclosure was subsequently had under the First and Refunding Mortgage, but no bankruptcy proceedings were had with respect to the owner of the property.

Upon that theory of the case appellant as representing general creditors of the corporation which form-

erly owned the properties is now seeking to recover the rental moneys which the Company applied to operating expenses and on account of obligations under the mortgage.

It is not believed that argument on this point on the part of the appellee receivers is necessary or desirable. Counsel for the receivers of Wardman Real Estate Properties, Inc. do not know of any reason why such moneys may be recovered.

Respectfully submitted,

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*Attorneys for Julius I. Peyser and
Joseph P. Tumulty, Receivers of
Wardman Real Estate Properties,
Inc.*

DOUGLAS, OBEAR, MORGAN & CAMPBELL,
Of Counsel.

UNITED STATES
COURT OF APPEALS FOR THE
DISTRICT OF COLUMBIA

FILED FEB 4 1938

IN THE

Joseph W. Starnes
CLERK

United States Court of Appeals
FOR THE DISTRICT OF COLUMBIA

No. 6963

EDWIN H. BROWNLEY, RECEIVER, WARDMAN REALTY AND
CONSTRUCTION COMPANY, *Appellant,*

v.

JULIUS I. PEYSER AND JOSEPH P. TUMULTY, RECEIVERS,
WARDMAN REAL ESTATE PROPERTIES, INC., AND
WASHINGTON PROPERTIES, INC.

**BRIEF ON BEHALF OF APPELLEE, WASHING-
TON PROPERTIES, INC.**

PAUL E. LESH,
Attorney for Appellee,
Washington Properties, Inc.

PEELLE, LESH, DRAIN & BARNARD,
Of Counsel.

February 2, 1938.

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BRIEF ON BEHALF OF APPELLEE, WASHINGTON PROPERTIES, INC.

Statement.

This brief is written in support of the position taken by the brief for the appellees Peyser and Tumulty, receivers, and as the facts are fairly consecutively stated in that brief, they will not be here repeated.

Interest of this appellee.

The appellees Peyser and Tumulty as Receivers have stated in their brief (p. 10), that they have no interest in the determination of the issues presented by this appeal except to perform their duty as officers of the Court, and that they do not wish to be considered as assuming a partisan position "in disputes between respective claimants". It seems to this appellee that in a case where as here the fund in the hands of the Receivers is sufficient to pay only about two per cent of the allowed claims, the assertion of any doubtful claim against the funds in the hands of the Receivers necessarily becomes a dispute between respective claimants, and that there is no question of the duty of the Receivers to resist a claim such as the present one which the Receivers are advised is not well founded.

This appellee, Washington Properties, Inc., is a corporation composed of former creditors, secured and unsecured, of Wardman Real Estate Properties, Inc. The bonds and stock of this appellee were issued in consideration of the transfers to it of first and refunding bonds of Wardman Real Estate Properties, Inc., of the entire debt secured by the general or junior mortgage of Wardman Real Estate Properties, Inc., and of two year notes of that Company. (Addition to Record) Though the process by which Washington Properties, Inc., came to be formed is conveniently referred to as a reorganization, pursuant to a reorganization plan with respect to Wardman Real Estate Properties, Inc., it might be more accurately described as an organization of *creditors* of Wardman Real Estate Properties, Inc., and Washington Properties, Inc. might well be conveniently termed the incorporated creditors, though not all of the creditors joined in its formation.

Washington Properties, Inc., acquired title to the *mortgaged* properties of Wardman Real Estate Properties, Inc., at the foreclosure sale under the deed of trust securing the first and refunding bonds (R. 24). The *unmortgaged* property of Wardman Real Estate Properties, Inc., has been reduced to cash (by sundry sales by the Receivers to appellee and third parties not shown by the record) and the Receivers hold the cash unmortgaged assets for distribution among the general creditors of Wardman Real Estate Properties, Inc.

The holders of approximately 93 per cent of the first and refunding bonds of Wardman Real Estate Properties, Inc., participated in the organization of appellee, Washington Properties, Inc. The trustee for the first and refunding bond issue obtaining a deficiency judgment for the benefit of all first and refunding bondholders in the sum of \$10,470,039.09, and the trustee's claim in that amount against the unmortgaged assets was duly allowed. The holders of the \$2,500,000 so-called general mortgage bond, junior to the first and refunding, and the holders of \$220,000 of two year unsecured notes, participated in the formation of Washington Properties, Inc., and it thereby became the owner of their claims, and as a claim by it on said bond and notes a total of \$2,270,000 was duly allowed against the unmortgaged assets (Addition to Record). Other claims, the amount of which does not appear by the record, were allowed against the unmortgaged assets. The unmortgaged assets now consist of a fund of approximately \$197,917.30 (R. 24, paragraph VIII).

No question is here nor can be as to the validity of the claims of this appellee against the unmortgaged assets. The allowance of them by the Special Master and its confirmation by the Court were without excep-

tion by any other claimant and have long since become final.

Therefore, though the Receivers assert only a somewhat academic interest in this controversy, this appellee is a party from the payment of whose claim a portion of the \$197,917.30 unmortgaged asset fund will be diverted if the present claim is allowed.

Argument.

The beneficial interest back of appellant's claim.

The appellant prosecutes this claim as the statutory receiver of an insolvent corporation (R. 28, paragraph XV). There is no proof as to who the creditors are on behalf of whom appellant is prosecuting this claim, how their claims arose and what their equities are.

In appellant's Assignments of Error (R. 48-49, numbers 2 and 6), and elsewhere in statements of appellant's position, the creditors who are beneficially interested in the claim prosecuted by appellant are referred to as "those who supplied services, goods, wares and merchandise in the normal course of business for the maintenance and operation of said properties", and the debts the payment of which are sought to be accomplished by the appellant are referred to as "current debts for the maintenance and operation of" the properties owned by the Properties Company and leased to the Construction Company.

If creditors of this description were here involved,—persons who extended credit relying on the apparent validity of the lease to the Construction Company, or relying on its possession of and control of the properties of the Properties Company while so leased,—a different question would be presented. Such creditors if unpaid could cite reason and authority in support of a

claim against the Properties Company. (See *infra* p. 26.) Whether appellant as Receiver of the Construction Company would be the appropriate claimant on their behalf would be doubtful, but that question need not be debated because it affirmatively appears from the record that there are no creditors of this description who might claim against the Construction Company and through appellant against the Properties Company's assets, as follows:

All parties to the appeal have agreed "that the statements of fact contained in the report of the Special Master contain a correct digest of the testimony adduced before him on the subject matter, except insofar, if at all, as they may be inconsistent with the agreed statement of facts" (R. 38, paragraph XVIII).

The Special Master's report states that the accounts payable by the Construction Company which were assumed by the Properties Company in the settlement of February 28, 1931, represented "all" of the ordinary trade accounts of the Construction Company (R. 36) and they have been paid by the Properties Company (R. 23). Nothing in the agreed statement of facts, and nothing brought forward by appellant in any way, is inconsistent with this finding of the Special Master.

What the record shows to indicate that any creditor of the Construction Company is unpaid or to be benefited by the claim asserted by the appellant is solely the following: About five months after the settlement and on July 31, 1931, a Baltimore court adjudicated the Construction Company insolvent and appointed the appellant statutory receiver (R. 28, paragraph XV). At the time of the settlement of February 28, 1931, the Construction Company had other assets not assigned to the Properties Company (R. 23, par. VI). Whether the

Construction Company had after February 28, 1931, by the operation of business relating to any other assets accumulated additional debts does not appear. It does appear that the Construction Company had as of September 1, 1928, issued \$2,500,000 of senior debentures and \$2,400,000 of junior debentures, on which it had paid all interest due up to February 28, 1931 (R. 24, paragraph IX), upon which it might be presumed additional sums were due by July 31, 1931, when it was adjudged insolvent.

When the Receiver of the Construction Company filed his claim May 6, 1933, he *alleged* that there were many outstanding and unsettled bills due by the Construction Company, none of which the Receiver could pay because all of its assets had been unlawfully taken by the Properties Company, but in the same sentence he also alleged that he was not informed as to what accounts payable by the Construction Company had been settled and discharged by the Properties Company (R. 32), whereas it is now agreed that the Properties Company has paid all of the obligations it assumed to pay under the settlement contract excepting a trifling account which was disputed and certain personal property taxes which have now been asserted otherwise than against the Construction Company (R. 23, paragraph VI). Appellant does not even assert that since its settlement with the Properties Company any claim has been made against it by any creditor growing out of the Construction Company's operation of the properties of the Properties Company. There is a complete absence of any showing as to what creditors are to be benefited by any allowance made to the appellant, and what their equities are, and no creditors are shown to exist excepting the holders of the debentures of the

Construction Company. As to these debentures, the senior ones were to be preferred in payment (R. 31), and of the senior issue of \$2,500,000, debentures totaling \$2,080,500 are held by this appellee (and as to the ownership of the balance the record is silent), and this appellee does not consider it to its benefit that any funds be routed to it through the Baltimore Receiver of the Construction Company. The debenture holders' proper claim on the assets of the Properties Company is through their security, the general mortgage \$2,500,000 bond of the Properties Company, and claim on it has been allowed (Addition to Record).

The nature of appellant's claim.

In the several places in the record and brief where appellant had opportunity to clarify the nature of his claim, there seems to this appellee to be such inexactness as to permit misunderstanding.

Thus in appellant's first exception to the Special Master's report, he refers to the denial of the "claim of said exceptant in the sum of \$186,656.52" (R. 39). His first assignment of error is in the same words (R. 48). His other exceptions and assignments of error merely state propositions of law believed to support his claim. The Special Master reported on the claim as one for this amount of money, made up of several items, but did not mention any distinction between the nature of this claim and that of the claims of creditors dealt with elsewhere in the same report (R. 35).

Nowhere in the record or brief is the claim described by pointing out that it is not what might be supposed from the foregoing, viz., that it is not a claim that the Properties Company is indebted to the Construction Company in the amount stated, but it is a fact that the

claim which appellant seeks to support in his brief would not be satisfied by the allowance of his claim in that amount as a creditor's claim. It could be satisfied only by a direction to the Receivers to pay him \$186,656.52 out of the total fund of \$197,917.30, leaving approximately \$10,000 to be ratably distributed among this appellee and the other creditors.

The order of the court below invited the filing of claims against the Properties Company or the Receivers "or against any property in the hands of the Receiver" (R. 26). The appellant's claim asserted the unlawful transfer and removal of practically the entire assets of the Construction Company into the assets of the Properties Company on March 7, 1931 (R. 29), and asserted that appellant "is entitled to be paid out of the cash in the hands of the Receivers" at least \$186,656.52 (R. 34).

Appellant in his brief (p. 5) refers to the order calling for the filing of claims and describes his own claim as one that out of the unmortgaged assets of the Properties Company appellant should receive an amount of money calculated by adding together several of the items thereafter dealt with. This was apparently intended by appellant as a claim against "property in the hands of the Receivers." It is an assertion of ownership of assets rather than a mere assertion of a right on the part of a creditor to his ratable share of assets to be devoted to the payment of claims of creditors.

The Special Master and the court below denied the claim upon the ground that there was no conversion of assets of the Construction Company by the Properties Company. Therefore it was held that appellant had no claim even as a simple creditor.

In order, however, to maintain the claim which appellant is actually asserting, that of ownership by the Construction Company of assets which the Receivers of the Properties Company took into their possession on their appointment July 14, 1931, it was incumbent upon the appellant to prove not merely a conversion of assets of the Construction Company by the Properties Company, which the court below held appellant had failed to do, but also to trace the assets which he asserted the Properties Company took as of February 28, 1931, into the funds and property taken possession of by the appellee Receivers on their appointment July 14, 1931.

To have proven a conversion below, without more, would merely have given appellant a claim which, though tortious in origin, would be a simple general creditor's claim in that amount and, if allowed, would pro-rate with those of other claimants.

In seeking to impress his claim on the assets taken over by appellee receivers, the appellant is certainly in no more favorable position than that of the cestui of a trust when a receiver has taken over the assets held by the trustee. Dealing with such a case, the Circuit Court of Appeals for the Eighth District, in *Empire State Surety Co. v. Carroll County*, 194 Fed. 593, 604, said:

“It is indispensable to the maintenance by a cestui que trust of a claim to preferential payment by a receiver out of the proceeds of the estate of an insolvent that clear proof be made that the trust property or its proceeds went into a specific fund or into a specific identified piece of property which came to the hands of the receiver, and then the claim can be sustained to that fund or property only and only to the extent that the trust property or its proceeds went into it. It is not sufficient to prove that the trust property or its proceeds went into the general assets of the insolvent

estate and increased the amount and the value thereof which came to the hands of the receiver."

This case is quoted as a leading one on this doctrine by Clark on Receivers (2nd Ed.), page 934, Section 662, and by Tracy on Corporate Foreclosures, Receiver-ships and Reorganizations, page 148, Section 131, by both of which texts claims for preferential payments by receivers are discussed.

American Law Institute Restatement of the Law of Restitution, page 866, Section 215, is as follows:

"Necessity of Tracing Property.

"(1) Except as stated in Subsection (2), where a person wrongfully disposes of the property of another but the property cannot be traced into any product, the other has merely a personal claim against the wrongdoer and cannot enforce a constructive trust or lien upon any part of the wrongdoer's property.

"(2) Where a broker wrongfully disposes of the securities of a customer, the customer is entitled to claim in substitution therefor securities of the same issue owned by the broker."

The same principle is frequently followed in bankruptcy proceedings. See *In Re Byrne*, 32 F. (2d) 189, 190, Circuit Court of Appeals, Second Circuit, 1929.

See also *American Can Co. v. Williams*, 178 Fed. 420, decided by the same court in 1910.

The appellant did not show that any asset of the Construction Company, of the conversion of which he now complains, remained in existence July 14, 1931, or that its proceeds identifiable as such were then taken into possession by the Receivers of the Properties Company. When the facts are examined, it becomes apparent that this was no mere oversight on the part of the

appellant, but that the assets transferred and now alleged to have been wrongfully converted had been wholly spent and consumed. In so stating we do not refer to the fourth or fifth items of appellant's claim as he enumerates them (R. 34), because as appears hereinafter (*infra* p. 12), these items of appellant's claim, are plainly eliminated for lack of proof. In reference to the other, the first three items of Appellant's claim, direct attention to the schedule of assets transferred (R. 20), and to the schedule of charges assumed (R. 21). The amount of cash transferred was \$61,392.01. Disregarding all accrued liabilities and taxes, the accounts payable which the Properties Company proceeded to pay and did pay (R. 23, paragraph VI) amounted to \$119,549.85. To pay these accounts almost \$60,000 had to be provided otherwise than out of the cash so transferred. Presumably some of it came out of conversion into cash of accounts receivable, of which there was a net of \$83,970.76. The other two items of assets taken over were inventories and prepaid items which of course were not capable of being converted into cash but were consumed and dispensed in the operations of the properties. The kinds of supplies included in the inventory item are shown in the schedule on page 21 of the record. It is not surprising, therefore, that no attempt was made by appellant to show that the assets he alleged were "lifted" from the treasury of the Construction Company and put into the treasury of the Properties Company on March 7, 1931 (as of February 28, 1931) or their proceeds were in specie taken into possession of Peyser and Tumulty five months later. Therefore, even if appellant could persuade this Court that the conclusion of the court below was wrong, and that there was a conversion of assets belonging to the

Construction Company by the Properties Company on March 7, 1931, appellant would be entitled only to have a claim allowed in the amount of the assets converted,—he would not have made out a case for a direction to the appellee Receivers to pay him the amount of his claim in full, irrespective of the sufficiency of assets in the hands of the Receivers to respond to other claims.

The amount and items of appellant's claim.

The appellant's total claim of \$186,656.52 is itemized in the final paragraph of his proof of claim (R. 34) into five items.

The fourth item, that of a "lien on the furniture and equipment at the Hay-Adams House, \$56,000," is apparently abandoned on this appeal. If this cannot be inferred from the lack of mention of it in appellant's brief, its abandonment appears compelled by appellant's agreement that the facts reported by the Special Master are supported by testimony (R. 38, paragraph XVIII), the Special Master's finding that Peyser and Tumulty as Receivers acquired good title to this lien claim, by transaction quite independent of the settlement of March 7, 1931, (R. 38), and the failure of appellant to bring forward any fact or consideration to the contrary.

The fifth items in the claim,—“unlawful payments on the Properties Company's properties within four months, \$25,000,” is likewise found against appellant by the Special Master, not only because the lease between the two companies reasonably required the Construction Company to make such expenditures while in possession as lessee and in receipt of all income from the properties, but also for lack of proof of the expenditures (R. 37, paragraph (2)). Nothing in the record is

inconsistent with this finding of the Special Master and the brief for the appellant mentions nothing inconsistent with it excepting the "sworn claim" of the appellant (brief, p. 16).

The remaining three items of appellant's claim, the first, second and third (R. 34) totaling \$105,656.52, appear to be those for which appellant is now contending. He refers to them in his brief (p. 3) as "liabilities" which were wrongfully balanced against assets transferred to the Properties Company in the agreement of settlement, though the third item "inventories, \$27,318.24" seems not to be a liability. Such contentions as appellant makes about these three items appear to be only those general contentions to the effect that corporate fictions are to be disregarded and intercorporate transactions between parent company and a wholly owned subsidiary set aside, which general contentions are hereinafter to be dealt with.

Appellant's contention that the fiction of distinct corporate entity is to be disregarded.

Appellant opens the argument portion of his brief (pp. 6-7) with criticisms of the original financing by the corporation of which he is Receiver and its controlled subsidiary, the Properties Company, and with statements to the general effect that the Properties Company and the Construction Company were in fact identical, as though he were arguing against any recognition of their separate existence and separate assets.

Appellant can hardly intend to push this argument to the extent that might be inferred from generality of his language, because to do so would defeat his claim. If the separate corporate identity of the two corporations were to be completely disregarded, and their as-

sets held those of one entity, subject to all the debts of both, then there would be no occasion to lift out of the assets administered here any funds for transmission to Baltimore for administration as the separate assets of the Construction Company. If such a complete unity exists that both corporate treasuries were (to use Appellant's phrase) "pockets in the same trousers," the Construction Company's creditors should be here claiming their proportionate share of whatever is in either pocket, and there is no occasion today to transfer anything from the Peyser and Tumulty pocket to the Brownley pocket.

In order to support his claim to recover anything herein, appellant must intend to confine his contention to a disregard of the particular intercorporate transactions which he attacks, viz., those connected with the settlement of February 28, 1931, and must maintain that there were and are separate entities and separate sets of creditors.

Appellant's contention that the settlement transaction is invalid.

In supporting appellant's proposition that the settlement of February 28, 1931, between the Properties Company and the Construction Company is ineffectual as to creditors of the Construction Company, appellant cites a number of authorities decided upon doctrines with which we have no quarrel either as abstract legal propositions or in their application to the cases decided. Only a few of these cases deal with creditors' rights, and they hold that under circumstances transactions between a parent company and a wholly owned company may be set aside as in fraud of creditors, and that any over-reaching practiced by the stockhold-

ing parent corporation upon the controlled corporation whereby the assets of the controlled corporation are made to benefit the stockholder, the parent company, to the damage of the subsidiary's creditors, is subjected to judicial scrutiny and may be set aside.

What is principally condemned in appellant's cases are stockholders' claims as creditors against corporations which by reason of transactions carried on for the stockholders' benefit have not sufficient assets to pay other creditors.

Thus the cases cited support what is the converse of appellant's proposition. Appellant's proposition is that here the wholly owned and controlled subsidiary disregarded the interests of its sole stockholder and over-reached the dominant owning corporation, and "lifted" the parent company's assets in fraud of creditors of the parent company. (The final clause of Assignment of Error No. 7, R. 49, illustrates appellant's curious inversion of thought about this.)

We do not rest our case, however, upon the inaptness of the cases cited by the appellant, because we concede that a dominant corporation might exercise its power over a wholly owned one by putting assets into the possession of the wholly owned corporation which might be held to belong, as against creditors of the dominant corporation, to it.

Dealing with the realities of the present case, however, it is our contention that the appellant cannot segregate the settlement agreement of February 28, 1931, from the immediately prior intercorporate transactions and attack it alone.

The Special Master found that the settlement transaction of February 28, 1931, was fair to the Construction Company (R. 37). This finding was affirmed by

the Court and, inasmuch as no fact in the Record contradicts it, it is doubtless sufficient basis for an affirmance by this Court of the denial of appellant's claim.

But the Record discloses what seems to us a more conclusive answer to the appellant's claim. The transaction of February 28, 1931, was merely in termination and cancellation of the lease of July 15, 1929, and necessarily the lease itself must be taken into account in any reexamination of the equities as between the two companies. When the lease was made and until the cancellation transaction, not only was the Properties Company wholly owned by the Construction Company, but the officers and directors were identical. In the making of the cancellation transaction, the respective companies acted through different officers and directors, and were advised by independent counsel (R. 15-16, paragraphs IV and V).

Before the lease of July 15, 1929, was made, the Properties Company owned and had been, since October 2, 1928, in possession of, the hotels, apartment houses and buildings which constituted its principal assets, and was itself in receipt of the income therefrom. Income was of course applicable first to cost of operation, taxes and other carrying charges, then to its obligations to the holders of the mortgages on these properties, which were (1) certain underlying mortgages,* (2) \$11,350,000 first and refunding bonds, and (3) the general mortgage \$2,500,000 bond (R. 4, 24, paragraph X). After these deductions from net income had been covered, the net income would have been subject to disposition, by way of dividend or otherwise, by the Construction Company as sole stockholder.

*These underlying mortgages are only mentioned in the Record, page 4, clause (3). Appellant's brief states that they amounted to \$5,000,000 and this figure is sufficiently close to accuracy to be accepted (Brief, p. 6, fourth line from bottom of page).

The Construction Company owned the general mortgage \$2,500,000 bond, as well as all of the capital stock of the Properties Company, and had pledged the same as collateral for its, the Construction Company's, senior and junior debentures (R. 24, paragraphs IX and X). Therefore, though entitled as stockholder to income of the Properties Company over and above its liabilities, the Construction Company could not properly so manipulate the situation as to take this income into its general assets. So to do would violate the rights of the debenture holders, who were entitled to be preferred or secured by a preservation of the value of the general mortgage bond of the Properties Company, which was pledged as collateral, and any routing of the income of the Properties Company direct to the Construction Company, otherwise than as the Construction Company might be entitled to a surplus above all debts through its holding of stock, diminished the security back of the debentures.

It is more obvious, of course, that any routing of the gross income direct to the sole stockholder, the Construction Company, was also a potential fraud upon all creditors of the Properties Company, and would become an accomplished fraud upon them when such gross income was applied by the Construction Company to the payment of its debts, leaving creditors of the Properties Company wholly or partially unpaid.

What the motives were which actuated the making of the lease of July 15, 1929, from the Properties Company to the Construction Company it is difficult now to determine; it is impossible to determine upon the present Record. It is clear that appellant's hypothesis, stated in his brief (pp. 6-7), that this lease was

the basis of the issue of the debentures by the Construction Company, cannot be accepted as satisfactory because the debentures had been issued September 1, 1928, almost a year theretofore, though it is conceivable that the lease may have been made to increase their apparent value. The lease purported to recognize that the income from the property should be applied first to the costs of operation and the requirements of the outstanding mortgages, for it provided that the rentals should be measured by them, leaving apparently, as the prospective profit to the lessee, no more than that to which the lessee would have been entitled as sole stockholder of the lessor.

If the lessee had paid the rent as agreed, the principal if not the only change worked in the relations of the parties by the making of the lease would have been that the net profit from the operations of the properties would have gone direct into the treasury of the Construction Company, instead of remaining among the assets of the Properties Company subject to the control of the Construction Company as sole stockholder. The Construction Company as lessee did not, however, pay the rent as agreed, and, after about a year and a half of operation, was in default to the amount of \$654,000, besides accrued real estate taxes amounting to \$47,000 (R. 16, paragraph III), besides which the Construction Company had incurred costs of operation, unpaid, amounting to \$193,048.72 (R. 21, Schedules E and F). In this situation the improper effect of the lease, if it were given effect as against creditors of the Properties Company (which because of insolvency of both companies, becomes very material,) would be that under the lease all accounts receivable, prepaid items, inventories and cash pertain-

ing to the operation of the properties were assets of the Construction Company and not of the Properties Company.

A lease from a wholly owned subsidiary of valuable income producing property to its sole stockholder, which has the effect of converting what would be assets of the subsidiary into a mere uncollected claim for rent against the insolvent stockholder, certainly cannot be defended against the then creditors of the subsidiary lessor. This appellee, Washington Properties, Inc., is assignee of persons who were then creditors of the Properties Company. (Addition to Record, XII.)

In dealing with the problem here presented, we commend to the Court's consideration the following comment from Ballantine, Manual of Corporation Law and Practice, page 29, Section 6:

“One situation in which courts sometimes speak of disregarding separate entity is that of the transfer by a corporation which is in debt of all its assets and business to another corporation having often a similar name and substantially the same stockholders and management. The real basis on which the creditors of the old can pursue the new corporation to the extent of the assets received is not because it is the same corporation under a different name, but on the principles of fraudulent conveyance, perhaps made somewhat more favorable to the creditor than if the transferee were an individual. It would seem that the creditors may proceed against the transferee without disregarding the corporate entity or identifying the grantee and the grantor, the corporation and its stockholders. The figurative talk about ‘piercing the veil’ or ‘stripping off the mask’ of a separate corporate entity does not help and the real questions involved are often thus obscured.”

Useful notes and cases under the topic "Disregarding Corporate Existence" are to be found in 1 A. L. R. 610 and 34 A. L. R. 597. The former one of these notes is begun with this comment:

"The distinction between a corporation and its stockholders is a legal fact, strong enough to carry property, though it is not unusual for the courts to speak of it as a fiction. * * * It is with due reserve, therefore, that we ought to consider such general expressions of opinion as those which immediately follow."

It will be found that cases which for the protection of creditors nullify transfers, contracts or arrangements involving corporations often speak of disregarding the fiction of separate corporate existence, but are decided, many of them, on general principles of agency and fraud not peculiar to corporation law, and insofar as they deal with doctrines peculiar to corporations and here material, give sharp effect to the respective rights of creditors and stockholders in property owned by the corporate entity.

For example, as to voidable transfers of property by corporate debtors, exactly as in the case of individual debtors, it is only creditors to whom debts are owed at the time of transfer who may complain, and as to whom relief will be granted. In *Graham v. LaCrosse & M. R. R. Co.*, 102 U. S. 148, 161, 26 L. ed. 106, 111, the Supreme Court said:

"A corporation is a distinct entity. Its affairs are necessarily managed by officers and agents, it is true; but, in law, it is as distinct a being as an individual is and is entitled to hold property, if not contrary to its charter, as absolutely as an individual can hold it. Its estate is the same, its

interest is the same, its possession is the same. Its stockholders may call the officers to account, and may prevent any malversation of funds or fraudulent disposal of property on their part. But that is done in the exercise of their corporate rights, not adverse to the corporate interests, but coincident with them.

“When a corporation becomes insolvent, it is so far civilly dead, that its property may be administered as a trust fund for the benefit of its stockholders and creditors. A court of equity, at the instance of the proper parties, will then make those funds trust funds, which, in other circumstances, are as much the absolute property of the corporation, as any man’s property is his. We see no reason why the disposal by a corporation of any of its property should be questioned by subsequent creditors of the corporation, any more than a like disposal by an individual of his property should be so. The same principles of law apply to each.”

Disregard of corporate title or of exclusive liability for corporate torts or debts is exceptional. *In Re Commonwealth Light & Power Co.*, 86 F. (2d) 474, 479, Circuit Court of Appeals, Seventh Circuit, November 1936, the court said:

“It may be stated as a general rule that, ordinarily, corporate existence can not be disregarded. *In Re John Koke Company* (C.C.A.) 38 F. (2d) 232, 233, the court said, ‘The rule is quite elementary that a corporation is an entity separate and distinct from its stockholders, with separate and distinct rights and liabilities; and this is true even though a single individual may own all, or nearly all, of the capital stock. True, courts, in exceptional cases, will look behind the corporate form in order to redress fraud, protect the rights of third

persons, or prevent a palpable injustice; but there is no reason for invoking any such exceptional rule here, because it is not claimed that there was fraud, concealment, or even ignorance of any material fact in the original transaction.' ”

The fact that one corporation was organized by those in control of another, with identical officers and directors, and with all stock owned by the other, does not establish such identity between them as nullifies their contracts or merges their properties and liabilities. In *Gillis v. Jenkins Petroleum Process Co.*, 84 F. (2d) 74, 79, Circuit Court of Appeals, Ninth Circuit, June 1936, the court, citing a number of cases, said:

“We see no reason to disregard the separate corporate entities of Western and Petrolgas. Much is made by Jenkins of the fact that the two corporations had common officers and directors and had offices in the same suite. It is also thought by Jenkins to be of profound significance that persons high in the affairs of Western procured the incorporation of Petrolgas. We are not impressed by these arguments. Wholly disregarding the undisputed testimony to the effect that an official of Graver Corporation, an affiliate of Jenkins, himself suggested the incorporation of a subsidiary for Western, we think it well settled law that the organization of one company by another, or the ownership of all the stock of one company by another, or common officers and directors, or all these elements combined, are not sufficient to defeat separate corporate entity.”

See also *McLean v. Goodyear Tire & Rubber Co., Inc.*, 85 F. (2d) 150, Circuit Court of Appeals, Fifth Circuit, August 1936; *Gledhill v. Fisher & Co.*, 272 Mich. 353, 262 N. W. 371, 102 A. L. R. 1042, September 1935.

There is, however, a type of transaction which is clearly vulnerable to attack by creditors of corporations, and that is, transfers or contracts by which corporate assets are passed on to officers or stockholders without payment of corporate debts. The vice of such transactions is not changed by the fact that the sole stockholder is another corporation. The basis of the rule is the simple principle that the stockholders are entitled only to the surplus *after* payment of debts. In the leading case of *Sawyer v. Hoag*, 17 Wall. 610, 623, 21 L. ed. 731, 736, Mr. Justice Miller speaking for the court said:

“It is very true that, by the power of the Legislature, there is created in all Acts of incorporation a legal entity which can contract with its shareholders in the ordinary transaction of business as with other persons. It can buy of them, sell to them, loan to them, and in insurance companies make contracts of insurance with them, in all of which both parties are bound by the ordinary laws of contract. The stockholder is also relieved from personal liability for the debts of the Company. But after all, this artificial body is but the representative of its stockholders, and exists mainly for their benefit, and is governed and controlled by them through the officers whom they elect. And the interest and power of legal control of each shareholder is in exact proportion to the amount of his stock. It is, therefore, but just that when the interest of the public, or of strangers dealing with this Corporation is to be affected by any transaction between the stockholders who own the Corporation and the Corporation itself, such transaction should be subject to a rigid scrutiny, and if found to be infected with anything unfair toward such third person, calculated to injure him, or designed intentionally and inequitably to screen

the stockholder from loss at the expense of the general creditor, it should be disregarded or annulled so far as it may inequitably affect him."

Federal cases illustrating and applying this doctrine are—

In re M'Carthy Portable Elevator Co., 196 Fed. 247, 251.

City of Fort Worth v. National Park Bank, 261 Fed. 817.

Wilkinson v. Livingston, 45 F. (2d) 465, Circuit Court of Appeals, Eighth Circuit, 1930, where the transaction held in fraud of creditors of a corporation was the assignment of a lease to a majority stockholder.

McCaffrey v. Elliott, 47 F. (2d) 72, 73, Circuit Court of Appeals, Fifth Circuit, 1931, where the court said:

"Generally, where a transaction is sought to be set aside on the ground of fraud, the rule is as stated by the District Court, but, while an officer or director of a corporation may deal with it the same as a third person, provided the transaction is in entire good faith, the rule as to proof of fraud is different. Such transactions are to be viewed with suspicion and scrutinized with care, and the burden is on the officer to show good faith."

Liquidators of Exchange National Bank v. United States, 65 F. (2d) 316, 317, Circuit Court of Appeals, Fifth Circuit, 1933, where the court said:

"It is undoubtedly the law that a corporation may not, as against its creditors, gratuitously transfer to, or incumber its assets for the benefit of, its stockholders or directors, or without consideration assume their obligations."

Bankers Trust Co. v. Hale & Kilburn Corporation, 84 F. (2d) 401, 403, Circuit Court of Appeals, Second Circuit, June 1936, where the court said:

“It is well settled that stockholders receiving substantially all of the corporate property of a corporation take it impressed with a trust in favor of unpaid creditors, any of whom may, to the extent of his claim, recover from any single stockholder the property so received or its value.”

To have permitted the lease from the Properties Company to its sole stockholder, the Construction Company, to continue after the Properties Company was entitled to terminate it for non-payment of rent, was, we submit, such a transaction as the foregoing authorities condemn. The gross operating revenues from the properties continued so long as the lease was left in effect to pour into the Construction Company's treasury, while the default under the lease grew to \$654,000.00, and other accounts payable connected with operations accumulated as indicated in the settlement schedules (R. 20-21).

When the settlement transaction is approached with these considerations in mind, it becomes apparent that the burden is on the Construction Company of showing that the settlement transaction restored to the Properties Company the assets it would have had but for the lease. As between the two corporations, the one in the fiduciary position, and to be required fully to account, was the Construction Company, not only because it controlled the other, but because it had exercised that control to take over all the income of the other. When these transactions are judicially reexamined, as sought by appellant, it is apparent that if there was any straining of the accounts to show a balance in the settlement

transaction, it must have been to protect the Construction Company from further accounting. The account as stated in the settlement agreement showed certain obligations assumed by the Properties Company which were to be balanced by the estimated value of assets taken over by the Properties Company. The assets taken over were a portion of the proceeds of operations which but for the lease the Properties Company would have had (R. 17). The balance was accomplished by ignoring the unpaid "rent", \$654,000. Had it been taken into account, the assets taken over would have fallen far short of balancing the obligations, and any comparatively small relief to the Properties Company by not being compelled to pay all the obligations assumed is therefore of no significance.

The true justification for the assumption by the Properties Company of the payment of the charges, which in the said settlement purported to balance the assets taken over, was that these charges were incurred by the Construction Company in the course of operations which were in truth, though not in form, operations on behalf of the Properties Company. When the lease as well as its cancellation are disregarded, these charges may properly be considered debts of the Properties Company. If any of them after the settlement had fallen on the Construction Company, or if any of them were now asserted against the Construction Company, its Receiver might have some basis of complaint. But the record shows that all of these debts were paid by the Properties Company excepting a trifling amount which was disputed, \$924, and some personal property taxes which are not being asserted against the Construction Company (R. 23, paragraph VI). Therefore the relief from further obligation on the part of the Construction Company growing out of its operations

under the lease, appropriate to be accomplished by the settlement transaction, was fully accomplished.

Such further facts bearing upon the fairness of this settlement as appear in the record give additional support to the conclusion that the Construction Company did not fully account in this transaction. It appears that while the lease was in force and the Construction Company was collecting all income from the properties of the Properties Company, the Construction Company, though it fell in default as to the agreed rental, was paying the interest due on its own obligations, the debentures (R. 24, paragraph IX). When the lease was cancelled February 28, 1931, the Construction Company was left in possession of other assets not assigned (R. 23, paragraph VI).

Appellant has not brought forward any proof of fraud practiced on the stockholder-lessee in the settlement transaction. He has, however, sought to surround the relations between the two corporations by a general cloud of fraud by references (brief pp. 7, 17) to the case of *Thomas et al. v. Central Hanover Bank & Trust Co.*, before this Court as No. 6011 April term 1933, reported in 64 App. D. C. 96, 75 F. (2d) 227. That case was here on a record which contained no evidence, and such views of the facts as were expressed by the Court and quoted by appellant were gathered from the pleadings and arguments. We doubt the propriety of reference to that case unless its doctrine of law was invoked as a precedent, and we ask no benefit of what there appears unless what appellant cites from that case is to be considered; but if reference is to be made to it, it will be found that present counsel for appellant signed as counsel a petition of his then client Alfred C. Torgeson (Record 6011, pp. 28, 36 *et seq.*) in which the

lease to the Construction Company was denounced as a fraud on the creditors of the Properties Company in terms more vigorous and with specifications of injury to the Properties Company's creditors and benefit to those of the Construction Company more detailed than are possible to this appellee because not appearing in the present record.

The cancellation of an arrangement which was thus operating to divert assets of the Properties Company and to make them appear to be assets of the Construction Company, with no more exaction from the Construction Company than is shown by the cancellation agreement, viz., the taking back from the stockholder-lessee of assets which were in truth assets of the Properties Company, appears not only to have been entirely fair to the Construction Company but probably very unfair to the Properties Company.

It is very clear that the record falls far short of containing anything showing that the lease and its cancellation, taken together, were any fraud on creditors of the Construction Company.

It is respectfully submitted that the judgment of the court below affirming the Special Master and denying the claim of the appellant was correct and should be affirmed.

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Washington Properties, Inc.

PEELLE, LESH, DRAIN & BARNARD,
Of Counsel.

UNITED STATES
COURT OF APPEALS FOR THE
DISTRICT OF COLUMBIA

FILED FEB 8 - 1938

Joseph W. Adams

CLERK

IN THE
United States Court of Appeals
FOR THE DISTRICT OF COLUMBIA.

No. 6963.

EDWIN H. BROWNLEY, STATUTORY RECEIVER, WARDMAN
REALTY AND CONSTRUCTION COMPANY, *Appellant,*

v.

JULIUS L. PEYSER AND JOSEPH P. TUMULTY, RECEIVERS,
WARDMAN REAL ESTATE PROPERTIES, INC., AND
WASHINGTON PROPERTIES, INC.

Appeal From the District Court of the United States
for the District of Columbia.

REPLY BRIEF FOR APPELLANT.

LESLIE C. GARNETT,
Attorney for the Appellant.

IN THE
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REPLY BRIEF FOR APPELLANT.

This brief is in answer to the brief of the appellee,
Washington Properties, Inc., and particularly to that
portion of the brief which, as we understand it, asserts

the doctrine that even though there was an unlawful conversion of assets of the Construction Company by the officers and directors of the Properties Company, nevertheless, it was incumbent upon the receiver of the Construction Company to identify the assets which came into the hands of the receivers of the Properties Company.

TRACING FIDUCIARY FUNDS.

It is pointed out that the court below merely sustained the finding of the Special Master. The finding of the Special Master was, as shown by the brief for the Washington Properties, Inc. (P. 8), that there was no conversion of the assets of the Construction Company by the Properties Company and therefore denied the claim. That was the sole question determined by the Special Master. There was no defense on the part of the receivers that none of the unlawfully converted assets came into their hands. It is significant too, that the receivers make no defense in this Court that they had in their possession none of the assets acquired unlawfully or otherwise by the Properties Company from the Construction Company. This contention remained to be made by the appellee, the Washington Properties, Inc., whose president upon its organization and now is the same individual who was president of the Properties Company and who so dominated the situation at the time of the unlawful conversion of assets that he designated the deferred and prepaid items which should be delivered to the Properties Company (R. 17); selected the operating accounts of the Construction Company, as well as the accrued liabilities which the Properties Company should pay, and with the President of the Construction Company

designated the accounts receivable and fixed the reserves therefor. (R. 18-19.)

It definitely appears in the record (R. 20) that assets of \$240,702.40 were diverted from the Construction Company to the Properties Company. Of this sum cash and accounts receivable amounted to more than \$150,000.00. Inventories, including the stock of goods in the drug store and the garage, amounted to more than \$27,000.00 (R. 21). Settlement between the companies was made on March 7, 1931, effective as of February 28, 1931 (R. 16). On July 14, 1931, the foreclosure suit was instituted and a few days after a general creditors suit was filed and they were consolidated (R. 21). It is undenied and undeniable that in these receivers proceedings inventories from the drug store and garage and the apartment houses and hotels as well as cash went into the hands of the receivers and the receivers now hold in the unmortgaged assets, more than \$197,000.00.

We have fully argued the question of the unlawful diversion of the assets of the Construction Company and shall not repeat it here. Granting, at least for the sake of argument, that there was an unlawful diversion, then it follows that the Properties Company held these unlawfully diverted funds in trust. It is well settled that no change of form can divest trust funds of the trust character, and the cestui que trust can follow and reclaim these funds so long as he is able to trace and identify them, not as the original property, but through and into any form into which the trust fund may have been converted. *Republic Supply Company, California, v. Richfield Oil Company*, 79 Fed. 2, 375.

The appellee, Washington Properties, Inc., relies upon *Empire State Surety Company v. Carroll County*, 194 Fed. 593, to sustain its contention that something more was necessary than to prove the unlawful conversion below. This case was a suit against the receivers of a national bank to require them to take from ratable dividends of other creditors of the bank the requisite amount to pay the County's claim in full. In dealing with this situation the Court used the language quoted in appellee's brief on page 9. The Court in that case, however, after stating the rule as quoted for the appellee, states the second rule as follows (p. 605) :

“Proof that a trustee mingled trust funds with his own and made payments out of the common fund is a sufficient identification of the remainder of that fund coming to the hands of the receiver, not exceeding the smallest amount the fund contained subsequent to the commingling, as trust property, because the legal presumption is that he regarded the law and neither paid out nor invested in other property the trust fund, but kept it sacred.”

Tested by the above rule, it is perfectly definite that when the Properties Company unlawfully diverted the more than \$240,000.00 of assets into its own treasury, these assets were commingled with its own assets. The presumption is that it retained these trust funds and kept them sacred, and when, at the end of four months, it delivered over to the receiver assets in excess of \$197,000.00, in these were the trust funds which it had unlawfully acquired. The rule is well settled that confusion does not destroy the equity entirely, but converts it into a charge upon the entire mass, giving to

the party injured by the unlawful diversion a priority of right over the other creditors of the possessor. *Frelinghuysen v. Nugent*, 36 Fed. 229. *Peters v. Bain*, 133 U. S. 670.

In *National Bank v. Life Insurance Company*, 104 U. S. 54; 26 L. ed. 693, 694, the head note written by Mr. Justice Matthews who delivered the opinion, is as follows:

“That so long as trust property can be traced and followed into other property into which it has been converted, the latter remains subject to the trust and that if a man mixes trust funds with his own, the whole will be treated as the trust property, except so far as he may be able to distinguish what is his own, are established doctrines of equity and apply in every case of a trust relation, and to moneys deposited in a bank account, and the debts thereby created, as well as to every other description of property.”

In the opinion (L. ed. 699) it will be seen that this head note is taken from the language of Vice Chancellor Sir W. Page Wood in *Frith v. Cortland*, 2 Hem. & W. 420.

In *Beard v. Ind. Dist. of Pella City*, 88 Fed. 375, 379, it is said:

“The foundation of the right on the part of the owner of a trust fund to a preference over general creditors in payment out of a fund or estate that has passed to the assignee or receiver of an insolvent person or corporation is that the trust fund has been wrongfully confused or intermingled with the property of the insolvent, or has been used to increase the value of property, thereby increasing the amount or value of the funds or estate passing into possession of the assignee or receiver; that if this intermingling had not taken place, the fund passing to the receiver would have

been so much less; that the creditors have only the right to subject the property of the debtor to the payment of their claims and therefore the creditors cannot complain if the total fund coming into the hands of the receiver is reduced by the amount necessary to make good to the owner of the trust fund the sum which was wrongfully used in augmenting the fund or property passing to the receiver. Unless it appears that the fund or estate coming into possession of the receiver has been augmented or benefited by the wrongful use of the trust fund no reason exists for giving the owner of the trust fund a preference over the general creditors."

Mr. Justice Cardozo in *Jennings v. U. S. Fidelity and Guaranty Co.*, 294 U. S. 216, 224, in discussing the substitution of other money for currency deposited in the vault of a bank, said:

"Not only that but a trust so created will not fail, though other dollars have taken the place of those already originally received, for dollars are fungibles and any one of them will be accepted as a substitute for another."

We, therefore, confidently submit that when the receivers acquired the inventories and moneys of the trustee, more than the amount of the trust fund which went into the hands of the insolvent, they are in no better position than the insolvent to say that the insolvent violated its sacred duty as a trustee and dissipated its trust fund instead of its own funds.

Indeed, the presumption that the Properties Company dissipated its own funds and not those it held as a trustee *ex maleficio*, is a rule of law which takes no account of the real intent. The Circuit Court of Appeals for the Second Circuit thus expresses the rule

in *In Re Kountze Bros.* 79 Fed. (2) 98, 101-2, (Certiorari denied in *Irving Trust Company v. Los Angeles*, 296 U. S. 640):

“The usual formula is to say that, where a fund is composed partly of the defrauded claimant’s money and partly of the fiduciary’s own money, the fiduciary is presumed to intend to draw out the money he can legally use rather than that of the claimant. *Central National Bank v. Insurance Co.*, 104 U. S. 54, 26 L. Ed. 693; *Cunningham v. Brown*, 265 U. S. 1, 12, 44 S. Ct. 424, 68 L. Ed. 873; *Knatchbull v. Hallett*, 13 Ch. D. 696. But, when courts speak of ‘presumed intent,’ they mean that a rule of law is announced which takes no account at all of the actor’s real intent. Equity marshals the withdrawals against the fiduciary’s own funds so long as it can because that result is deemed fairer. There is good reason for this because the fiduciary’s creditors have accepted the risk of his solvency, while his cestuis have accepted only the risk of his honesty. If this be the underlying reason for the rule, as we believe, it should apply not only to the collected deposits, but also to the uncollected. The credit which the bankrupts were privileged to use without defrauding any one they should be deemed to have drawn against, rather than against funds held in trust for persons who relied upon their honesty.”

To the same effect is *Scully v. Pacific States S & L Co.*, 88 Fed. (2) 384, 386-7.

BURDEN OF PROOF SHIFTED.

The books of the insolvent trustee and any evidence to show that in the four months intervening between the unlawful conversion and the receivership, the trustee violated its duty is wholly within the knowl-

edge of the receivers. Having established the trust fund, the lien must be impressed upon the commingled funds, unless the receivers who have the laboring oar can show a dissipation of those funds. *Scully v. Pacific States S & L Co., supra*, (p. 387).

This is not a contest between depositors in a Bank where each contributed to the fund on deposit. The question here is between the general creditors of a corporation which acquired large assets of another corporation under circumstances making the first corporation a trustee *ex maleficio*. As has been said above, the one class depending only upon the solvency of the corporation, the other upon the honesty of the officers and directors.

We insist that the strict rule as to tracing funds has long been supplanted by a more liberal one and that no change of form can divest the trust fund of its trust character and that, therefore, if the original stock of goods and inventories which the Properties Company unlawfully diverted to itself had been converted into other goods, wares and merchandise at the time the receiver took them over, this is a wholly sufficient tracing of the original inventories. Likewise, having traced into the hands of the trustee more than \$150,000.00 in cash and bills receivable, the receivers will not be heard to say that the trustee violated his sacred duty and dissipated this trust fund, and that the more than \$197,000.00 which the trustee had on hand was the trustee's money and not that of his cestui que trust.

In any event, having traced trust funds into the hands of the trustee, having shown the commingling of those trust funds by the trustee with his own funds, certainly the injured cestuis que trust are entitled to

an accounting from the trustee or from the receiver which they have never had and which was denied to them on the sole ground that there was no unlawful diversion of their funds toward the Properties Company. When a trustee commingles trust assets with his own, "the whole will be treated as the trust property except so far as he may be able to distinguish what is his own". *National Bank v. Life Ins. Co. supra.*

The interposition of a receiver does not shift this burden away from the trustee.

OTHER CONTENTIONS OF THE APPELLEE.

The appellee complains that there is no proof as to who the creditors are on behalf of whom the appellant is prosecuting this claim. This is a matter wholly for the consideration of the Court of the State of Maryland under whose authority the appellant is acting. It clearly appears, however, that there are bondholders and debenture creditors who are certainly entitled to some consideration when the assets of the Construction Company are unlawfully dissipated.

Complaint is also made that exceptions were taken to the denial of the whole claim of the appellant in excess of \$186,000.00, while the claim is asserted for a lesser sum. Certainly it is not to be expected that the assignment of error would be for less than the appellant felt might be the amount under a full accounting which should be distributed to the creditors of the corporation for which he is receiver.

However, the theory of the claim of the appellant is that in equity the trustee would be entitled to a credit for all of the debts of the cestui que trust which he actually paid and, therefore, taking the settlement be-

tween the corporations at its face value, in the brief for the appellant and in the absence of a full accounting, we have asserted that the appellant is entitled at least to the difference between the \$240,000.00 assets which the trustee unlawfully acquired and the amount which the settlement shows the trustee might have paid out, and this evidences a misappropriation by the Properties Company of \$105,885.37.

In conclusion, we reiterate that it remained for the appellee, Washington Properties Company, who not only acquired all of the real estate of the receivership at a "grossly inadequate" price, but who now holds a \$10,000,000.00 deficiency judgment in these proceedings and who will get almost the entire unmortgaged assets under the decree below, to draw the red herring across the trail, that the burden is upon the injured cestui que trust to prove that the trustee did not dissipate the trust funds, when nearly \$200,000.00 of the mass of commingled funds and assets were turned over to the Receivers.

Respectfully submitted,

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